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# INTRODUCTION

The purpose of this *Improved Budgeting Practices Manual* is to provide cities in Poland with information on how to use the budget as a policy, management, and communication tool. In light of new responsibilities given to cities in Poland and limited resources to provide services, it is imperative that cities manage their resources as best as possible. In order to do so, the budget has to be looked at as not only an accounting tool, but also a resource for management and decision-making.

Generally, the *Manual* addresses the development of a program budget, which strives to allocate funds based on stated public goals and program priorities rather than specific line items in order to assess the efficiency and effectiveness of services provided. A program budget is one example of how the budget can be presented to provide decision-makers, citizens, creditors, and others with a clear understanding about how resources are being spent and the results that are being achieved.

In Poland, cities are required to report their budgets to the state in a specified format. But, cities are also allowed to add information to the budget presentation beyond the minimum requirements. This flexibility has allowed cities such as Szczecin, Lublin, and Krakow to add sections to the budget to further explain programs or to actually present the budget in a second format. The purpose of the additional, or reformatted, information is to give those reading the budget a clearer understanding of how money spent relates to services provided.

The *Improved Budgeting Practices Manual* consists of fourteen chapters that give a step-by-step presentation of the budget preparation and implementation process and an elaborate case study of the changes made in the budget process in the City of Krakow. Chapter 1 presents an overview of the Multiple Purposes of Budgeting. Chapters 2–14 cover Budget Planning and Policy Development, Budget Preparation, and Budget Approval and Implementation. These chapters include practical exercises to apply concepts presented as well as examples from both Polish and U.S. cities. The final section of the manual includes a detailed description of the experience of the City of Krakow during the last three years as well as exercises based on current budget practices.

The *Improved Budgeting Practices Manual* is presented in a binder format because it is meant to be a working document. Readers are encouraged to make suggestions for improvements and to contribute case studies based on the experience of their cities for consideration.

It should be noted that when the budget is used as a policy, management, and communication tool, the budget format will be unique to its city because of preferences of staff and council members, technological resources, citizen demands, and other factors. The *Improved Budgeting Practices Manual* is meant to present a guide from which to choose elements that are most appropriate to your city, and not a prescription to be followed to the letter.

This *Manual* was prepared by the International City/County Management Association (ICMA) in collaboration with the City of Krakow. Chapter 1 was written by ICMA consultant Philip Rosenberg for the 1994 Municipal Finance and Budget Conference, which was attended by local government representatives from eleven countries. Chapters 2 –14 were written by ICMA consultant Winston Evans in preparation for a series of training workshops to be conducted in Poland using the manual. The Krakow Case Study was written by City of Krakow staff Jan Filas and Izabela Kozinska with contributions by Deputy Mayor Krzysztof Pako\_ski. Funding for the manual was provided by the United States Agency for International Development (USAID) under the Local Government and Housing Privatization Project for Central and Eastern Europe (Contract No. EUR-0034-C-00-2034-00, Requests for Services #125 and #92).

# CHAPTER 1

## MULTIPLE PURPOSES OF BUDGETING:

### THE BUDGET AS A POLICY, MANAGEMENT, AND COMMUNICATION TOOL

#### PURPOSE

The purpose of this chapter is to:

- Provide a broad overview of the multiple purposes of budgeting
- Introduce the concept of using the budget as a policy, management, and communication tool
- Present a summary of the components of the operating budget.

Budget policy begins with budgeting, a complex and ill-understood human activity. Budget policy guides the activities of people who are budgeting. To understand budget policy and its limits, a basic question must be addressed: What is a budget? The traditional definition expressed in the literature is one that classifies the budget as a financial plan for a municipality. Budgeting is the process of preparing and implementing the locality's financial plan.

The budget function in many municipalities around the world is restricted to estimating the cost of providing current services, allocating funds throughout the organization, detailing the categories of expenditure, and monitoring specific expenditures. This *control orientation* of budgeting evolved from the desire to fix spending and taxing levels in order to constrain impulsive and unplanned spending.

Several factors have changed the environment in which local government budget practices operate, expanding the role of the budget beyond a simple control tool. These changes have resulted in increased emphasis on making the budget a vehicle to articulate municipal fiscal and program policies and to communicate these policies to a diverse audience.

In Central and Eastern Europe, many functions have been transferred from central government to local governments over the past several years. With this shift has come responsibility to raise revenue, allocate resources, and monitor government operations. The significance of the municipal budget has expanded as governments are increasingly being challenged to maximize

resources and improve managerial productivity and accountability. Policy-makers, the investment community, and citizens are demanding timely and accurate information on government policies, operations, programs, and expenditures. In response to this challenge, public officials are seeking cost effective approaches to service provision, productivity improvement, and budgetary control.

More than ever before, municipal leadership must effectively allocate community resources. Chief executives, legislators, and local government staff must understand the role fiscal decisions play in serving the community. Decision-makers (mayors and city councils, department heads, and budgeteers) must respond to the following kinds of questions:

- Given the shift in responsibility for the provision of services, how should the local government organize to accept this responsibility?
- What programs and services need to be initiated? What must be eliminated?
- Does the local government have the organizational and staff capacity to manage these responsibilities?
- Can the municipality afford these programs and services?

The budget process is the forum within which these and other critical questions are posed and, hopefully, answered. Budgeting is the mechanism to debate policy options and consequently formulate policies in response to community needs and changes. The result of this effort is the adoption of the municipal budget.

Budgeting requires making difficult decisions about where to place limited financial resources among competing needs. While needs may be great, revenues will likely be insufficient to meet all those needs. Government officials must identify the current and future community environment; define needs; establish goals, priorities, and strategies to meet those needs; and wisely allocate resources.

The budget has evolved from a reporting of numbers, a barely distinguishable and often misunderstood statement, to a multi-faceted document. For many local governments, the budget is the single policy document that articulates the government's fiscal and program policies and explains the rationale for these policies. In addition, the budget is:

- An operations guide that provides guidance to department managers and measures the department's productivity
- A financial plan that provides a comprehensive perspective of the government's financial condition over a period of time

- A powerful communication tool that brings valuable information to the citizens, business persons, those considering making investments in the community, central government officials, and others.

This paper describes the process of moving the budget from a control document to a statement of a community's fiscal and program policy. It also offers some tips on how to assemble a budget document that is a powerful communication tool.

## A MOVE FROM THE TRADITIONAL BUDGETARY APPROACH

The control orientation to budgeting is reflected in the *line-item budget*. The focus of the budget is *what is bought?* Expenditures are organized primarily by objects of expenditure such as salaries, materials and supplies, and goods and services. While easy to prepare, the line-item budget does not provide any information regarding activities and functions of a program, department, or city. Dissatisfaction with the line-item budget, and its emphasis on inputs and controls, plus increasing demand from citizens and investors to understand the services and programs provided by local government, has led many municipal officials to seek budgetary reform.

To make more informed policy decisions and communicate budgetary decisions, municipalities have increasingly adopted budgets that blend the characteristics of the following two budget types.

- Instead of looking at what a municipality purchases, the *program budget* allocates money to major program areas rather than to specific line items. It seeks to identify the effectiveness of financial and program investments. The focus here is *what is achieved?* Thus, it is an attempt to classify governmental activity by goals and objectives, stressing the end product as opposed to the means. The advantage of this approach is that it is easier in analyzing a budget to grasp quickly the relative emphasis being given to a particular program as compared to alternatives, regardless of the number of agencies affected or activities involved.

- In *performance budgeting*, expenditures are based primarily upon measurable performance of government activities. It seeks to measure the efficiency of government operations. The emphasis is on *what is done?* The goal is to relate the input of resources to the output of services. Performance data are used in preparation of the budget as a basis for increasing or decreasing the amounts of resources devoted to various functions. The underlying theory of this approach is to shift the focus of budgetary decisions from inputs (i.e. salaries and other services and goods) to outputs (i.e. program results). In reality, performance budgets are difficult to fully implement because of the inability of many financial systems to generate unit cost and performance data need to fully evaluate performance. As a result so-called performance budgets often include traditional objects of expenditure with performance indicators.

In reality, there are as many budget formats as there are budgets. Budgets may blend elements of each of the three budget formats described above. What is important is that the budget serve as the managerial plan of action for the municipality.

## **SETTING THE POLICY: EXECUTIVE AND LEGISLATIVE GUIDELINES**

Budget preparation flows from the policies established to guide the budget process. Crafting a budget preparation policy includes the following elements.

At the beginning of the annual budget preparation cycle, the chief executive (e.g. mayor, chief administrative officer, city manager) or budget officer should initiate discussions with the members of the legislative body concerning the principal policies which should be reflected in the budget. To develop these policies it will first be necessary to review current fiscal conditions and the prospects for the coming or budget year. This *top down* approach is based on the chief executive's examination of:

- Current revenue performance and preliminary estimates of revenues for the budget year
- Current expenditures versus budget and the prospects for a surplus carry over into the budget year
- Trends in inflation and local economic condition
- Prospects for new taxes and fees or changes in current tax and rates
- Major cost items which will fall due in the budget year.

The objective in this analysis is to develop a rough framework of the financial constraints that will be faced in the budget year.

Next, a discussion should be conducted to develop some ideas regarding the scope of services that should be reflected in the budget. Based on these discussions, some basic policies to guide budget development should be set forth. Some policies might include:

- Guidelines for budget increases due to inflation
- An indication of what service areas should be strengthened, de-emphasized, or eliminated
- A statement of tax and fees policies to be followed.

These overall budget policies should be formally endorsed by the legislative body and disseminated to all appropriate administrative officials.

The governing body or legislature should concern itself with overall budgetary and program policy. Its members can be most effective when they use the budgetary process to establish the scope and direction of municipal services. The governing body may also establish budget priorities through a goal-setting process. In adopting the budget, the legislative body sets out the policy and direction a municipality takes in its efforts to deliver services to the citizens.

## **PREPARING THE BUDGET**

### **Chief Executive**

The chief executive has three major roles in the budget preparation process:

1. Preparing budget proposals for consideration by the legislative body
2. Explaining and clarifying current fiscal conditions, fiscal prospects, and budgetary proposals to the legislative body
3. Implementing the budget enacted by the legislative body and monitoring performance to ensure that programmatic and fiscal policies are met.

In smaller local governments, the chief executive may be responsible for each of these areas. In larger municipalities, a budget officer or chief financial officer assists the chief executive to meet these responsibilities.

While the executive role in local budgeting should always encompass the above responsibilities, the manner in which the executive function is organized may vary considerably. In some local governments, department heads deal directly with the legislative body. This is particularly true where each member of the legislative body is assigned responsibility for direct oversight of a particular department. It is recommended, however, that all executive budget functions be administered by a single executive official. This will ensure that: (1) there is consistency in budget preparation and format among municipal department budget submissions; (2) legislators will have a focal point to guide the establishment of municipal policy; and (3) priorities for services will be determined from a central vantage point.

## **Budget Officer**

The budget officer plays a key role in budget preparation by serving as a focal point for issuing guidelines, reviewing materials, and responding to questions. The budget officer's role may be of three general types. First, the budget officer may serve simply as a coordinator of budget materials. Second, the budget officer may perform a significant policy guidance function. In this role, the budget officer not only performs all the coordinating tasks, but also becomes involved in all the programmatic and financial issues relating to the budget. He/she assumes analytical and guidance functions such as:

- Issuing guidelines to departmental officials regarding acceptable level of service increase or decrease and expected cost limitations
- Evaluating departmental requests and adjusting them to policy guidelines
- Balancing expenditure requests with available revenues
- Making recommendations for budget action to the legislative body.

In the third type of role, the budget officer assumes responsibility for direct supervision over budget implementation. Specific tasks include:

- Ensuring that departments do not exceed budget limits by conducting periodic projections of expenditures and comparing them to available resources
- Maintaining centralized position control to ensure that personnel are hired only into an authorized position and at a salary no greater than the amount designated in the budget
- Reviewing and approving all requests to transfer funds from one budget to another
- Preparing reports on budgetary performance for the use of the legislative body, chief executive, departments, and citizens
- Closely monitoring departmental performance to determine potential problems.

## **Agency and Departmental Budget Requests**

The people who manage local activities should be involved in the budgeting process. This simple principle seems obvious; however, in a great number of cases a chief executive (or budget officer) prepares budget requests without much prior discussion of that budget with departmental managers who must operate under it.

Department heads must be involved in the details of budget development and implementation. Budget requests for each service should include a determination of what the service is; what

level of service has been provided in the current year; what level of service is needed in the budget year; what will happen if the service is reduced, discontinued, or increased; and the cost of service at the requested level. This information can be conveyed in an informal way or through a formal statement of specific objectives and workload measures, and through presentations of alternative service levels.

Department heads must also seek to summarize these details and present information in a way that complements the legislative policy making function. The budget requests they generate will trigger a round of budgetary policy decisions which, in turn, affect resource and spending levels, and modify or alter original budgetary goals.

## **BUDGET REVIEW AND ADOPTION**

### **Review by Municipal Officials**

The chief executive (or budget officer) is in the unique position of reviewing all requests and must thus be prepared to establish priorities in light of major issues or potential fiscal problems facing the local government. The review of departmental submissions should focus on ensuring that proposals are consistent with the budget policies established at the beginning of the budget process. Beyond this, the chief executive will have to make many difficult, and often unpopular, decisions. Typically the sum of all budget requests will exceed the total of estimated revenues plus any estimated surplus from the current year. Competition among departments and programs for access to limited governmental fund sources becomes inevitable. Tough choices will have to be made, but these choices should be made in the context of overall municipal program and fiscal policy.

The legislative body should be sure that it receives all the materials it needs to give full consideration to the budget proposals presented by department heads. For local officials to achieve the most effective policy making role, the budgetary materials they receive should permit them to gain a comprehensive understanding of local financial conditions, revenue prospects, and alternative uses of local funds in the provision of services.

The legislative body should not concern itself extensively with the administrative and financial details underlying the budget. While poring over the details of the budget, legislators can lose sight of important programmatic and financial issues embodied in the budget proposals. In particular, the legislators should avoid becoming overly involved in considering minor expense items. Such an approach is undesirable because:

- It may foster false economy—small amounts of money may be saved, but the fulfillment of service objectives may be impaired; or
- It wastes the valuable time of legislators on insignificant aspects of the budget.

A technique that some local legislative bodies have used to enhance legislative involvement in the budget process is selecting a finance committee from its members to work closely with the chief executive and department heads to develop the budget. This committee also monitors budget implementation and reports progress back to the full legislative body.

### **Review by the Citizens**

Since the budget is the community's policy tool, a conscious effort must be made to determine what the citizens think about current policies and services, including where they think services could be strengthened, and what levels of priority they attach to various services provided. Frequently, local officials rely largely on the perceptions of departmental management or the most vocal citizens to establish budget policy and service priorities. In both cases, the real preferences of citizens may be distorted. A more systematic approach to understanding citizens' needs should be undertaken using techniques such as holding hearings on specific budget policies and service priorities.

Another method is to go to the citizens. Explain the kinds of services for which the city is responsible. Discuss municipal fiscal and program policies and obtain feedback. As noted below, once the approved budget is assembled, make the document available to the citizens.

### **Adoption**

Once the proposed budget is introduced, and reviewed by the legislative body (and the general public), it will likely undergo more changes until it is adopted by the legislative body. Adoption of the proposed budget by the legislative body establishes the legal authority for administrative officials to incur expenditures in the budget year. The adoption of the proposed budget is the culmination of an exhaustive review of budget proposals by the legislative body and the chief executive.

## **THE OPERATING BUDGET DOCUMENT**

A diverse audience will be interested in the municipal budget. Beyond the municipal policymakers, staff and citizens, the investment community and business communities are interested in the budget. To this audience, the budget document represents the business plan of the community. It presents the community's investment strategy and financial resources. What are the community's priorities? What economic activity will likely result from the budget? Do these investments create an environment within which a given business will prosper? How prudently is the city managing its precious limited financial resources? If done properly, the budget document can answer many of these questions and attract investment interest in the community.

How best to present the budget? In order to understand a budget, the reader needs to know what type of data is contained in the budget document, as well as why it is in the document. A suggested outline for budget presentation includes:

- Policy Overview
- Organizational and Community Profiles
- Financial Summaries
- Operating Detail.

## **Policy Overview**

Underlying the budget's myriad of financial data, statistics, and narrative are decisions concerning program, revenues, and spending priorities. The policy overview explains the numbers. It is a summary of the decisions made, the factors which led to them, and their implications for programs and services. This section of the budget articulates issues and problems of special concern to the municipality, budget goals and priorities, links past and future budget activities to the current budget, and discloses the assumptions upon which budgetary decisions and estimates have been made.

Many different assumptions underlie budget decisions and estimates. Assumptions are an integral part of revenue estimates. For example, locally generated revenues are based, in part, on how much a particular tax base will expand or contract during the budget year. Budgets should disclose assumptions associated with this growth and decline. Policy makers can then decide whether such assumptions are reasonable. Budgets also should disclose assumptions underlying major policy and spending decisions. For example, budgets should disclose changes in service demand or economic vitality that result in major shifts in service levels.

Budgets are not created in isolation: they are influenced by prior budgets and serve as a precursor to future ones. The best budget documents highlight the historical significance or prior years' plans and set forth both short-term objectives and long-term goals and strategies. If done properly, the short- and long-term views will establish a bridge between budget years.

The actual content of a policy overview will vary considerably from one year to the next. As a result, there is no specific formula for preparing a good overview. However, the policy overview may include the following items common to most overviews.

•**The budget message/transmittal letter.** This is a one- or two-page letter that introduces the policy discussion. It formally conveys the budget document to the legislative body and serves much the same purpose as does a cover letter of any official report. Although not an essential ingredient, the transmittal letter may summarize key budget decisions or serve as an extensive budget message. A comprehensive budget message can satisfy all of the objectives of the policy overview. A simpler message can serve as an executive summary for the document. The best budget messages, however, always articulate goals and priorities. They describe fiscal and program strategies to address pressing issues and help a government fulfill its mission. In

an executive budget, the budget message outlines the chief executive's or administrator's budget agenda.

•**The time perspective: short-term objectives and long-term goals.** The budget should be presented in the proper context, and its connection with past trends, current events, emerging issues, and future directions should be explained. Generally, financial or programmatic goals have either a short- or long-term focus and relate to single programs or an organization as a whole. It is uncommon for a significant budget issue to have a life span equal to a single budget year. Major issues, such as economic downturns and privatization of housing, are likely to span several budget cycles.

Budget goals come in many forms, including annual goals and objectives, key issues, program strategies, strategic plans, and financial policies. As appropriate, the budget also should identify policies that are expected to continue in effect for a number of years, varying little from year to year. These are multi-year policies that seek to achieve broad goals (e.g. to maintain and enhance the employee work force by providing appropriate pay, training, and technology support to maximize employee productivity).

•**Organize along major themes.** Successful policy overviews are constructed around major themes that are action-oriented statements. For example, one theme in a budget message can be "Making Our City a Better Place to Do Business." Another theme might be "Improve the Health and Safety of Our Citizens." Effective themes link separate and distinct parts of the budget into a cohesive document. For example, the "Making Our City a Better Place to Do Business" theme would be highlighted in the budget message, and then detailed with individual agency and program narratives. If carefully prepared, budget themes can communicate both issues and goals to a wide range of audience.

•**Illustrate with graphics.** Graphics can make a strong message even more powerful. Where appropriate, themes should be illustrated with graphs and charts. They reinforce messages through a visual depiction of trends, projections, and current conditions. Policy themes should be backed by appropriate economic, financial, and program data. For example, a fiscal austerity theme could be best supported by details on those economic and financial events or trends that led to those consequences. Sometimes a simple reference to data and statistics contained elsewhere in the document is sufficient. In other cases, including a summary table may be appropriate.

Note that a well-written policy overview recounts decisions made during the budget process and expresses them in a coherent and concise manner. However, even the best-written overview cannot compensate for short-sighted policies or budgetary inaction.

## Organizational and Community Profiles

Certain factors consistently influence the budget. Some are internal, such as organization al structure and the budget process itself; other are external, such as the economy and demo-graphics. Factors which have a major influence on the budget from one budget period to another should be highlighted separately within the document.

Organizational and community profiles describe a government's organizational structure and staffing; explain a government's financial structure and budget process; and highlight the demographic, economic, and cultural features of the community served by the government.

The profiles should describe the organizational structure and financial structure. Include an overview of the government's functions and programs. Agencies and depart ments responsible for carrying out these functions and their relation ships should be explained. Since personnel costs are a major portion of the budget, provide a summary of staffing and a staffing history.

This section of the budget document should explain the government's fund structure and the budget classification used to categorize resources and spending. In addition, the profiles should include a description of the budget process, including preparation, adoption, and imple-mentation stages.

Highlight demographic, economic, and cultural features in the profiles. Programs and services financed through the budget will be influenced by community needs and prob lems; therefore, the budget narrative or statistics should highlight distinguishing charac teristics of a jurisdiction, such as cultural diversity, major elements of the local economy, and physical assets.

A combination of graphics, statistics, and text can be used to achieve the objectives of this section of the budget. The essential features of an effective profile include the following:

•**Organizational chart.** The most common means of displaying organization structure is the organizational chart. These charts help the reader visualize the structure of the govern ment and the relationships within it. Staffing summaries, which identify person nel or position counts for each department or program, also may be included.

•**Community profiles and statistics.** The budget should profile the community served by the government. Some categories that may be included in the profile include:

- Brief history of the community or government
- Form of governance
- Land area
- Population
- Income and employment trends
- Land use
- Major employers

- Condition of housing stock.

The biggest challenge in preparing organizational and community profiles is determining the proper amount and placement of the information. In many cases, profiles are treated as an afterthought. Statistical information, in particular, is often used inappropriately. All too frequently, statistical information is chosen because of its availability, not its relevance. In addition, this data usually ends up at the end of the budget because there is no other place to put it. Since the intent of these presentations is to allow the reader to quickly grasp the major budgetary issues, trends and choices addressed in the budget, it is recommended that profiles underscoring the significant aspects of the budget policy adopted be integrated with the transmittal letter.

## Financial Summaries

The financial summary section of government budgets summarizes information contained in the operating detail section. It also may include information not presented elsewhere in the document.

At a minimum, most financial summaries present a consolidated budget summary, cross-classify financial data, and present information on revenues, expenditures, capital spending, and debt.

The five basic types of financial summaries found in budgets are consolidated summaries, revenue summaries and analyses, summaries of current expenditures, capital spending summaries, and debt summaries. For each type of summary there are many variations. Presented below is a brief description of each summary.

•**Consolidated summary.** This summary displays all financing sources and uses. It includes information on revenues, transfers, debt proceeds, expenditures, and beginning and ending balances.

•**Revenue and expenditure summaries.** These types of summaries show greater detail than a consolidated summary. Revenue and expenditure summaries should include prior year actual, current year budget or estimated current year actual, and proposed budget year revenues and expenditures, by source or revenue and major expenditure category.

•**Capital spending summary.** Major capital projects benefit a government and community as a whole and require a long-term commitment of funds. In the United States, many local governments budget separately for capital improvements such as the purchase of land, major physical facilities and heavy equipment. These projects are different from activities related to government operations. Some inherent characteristics of capital projects have become reflected in the ways that local governments budget for them:

- Most capital projects not only involve substantial expenditures but take several years to complete. The purchase of a site or signing of an architectural contract implies greater expenditures in subsequent years for construction, equipment, and furnishing.
- Most localities have the capacity to finance only a limited number of capital projects in a given year. For example, the community may be able to budget for street or sewer construction in only one neighborhood in a given year, even though it recognizes that other neighborhoods have needs that are almost as pressing.
- The capital budget tends to be an important element of the locality's long-range planning and development. Its future year implications are critical to factors such as future operating expenses and community growth and change.

Each of these characteristics of capital projects tends to require multi-year thinking about the capital budget to a greater degree than most local officials feel is required, or even possible, with respect to the operating budget. The important role played in capital budgeting by multi-year planning usually results in the preparation of both a single-year capital budget and a multi-year capital program for the succeeding three to six years.

As a result, capital spending information is shown separately from the operating detail. The capital spending summary should include the following information:

- A brief description of major capital projects authorized in the budget
- Budgeted appropriations for these capital projects, including sources of financing such as taxes, user fees, central government loans and grants, and borrowing from banks or other lenders
- A brief description of the capital planning and budgeting process and its relationship to the operating budget
- The estimated fiscal impact of these capital projects on current and future operating budgets.

**•Debt summary and analysis.** The last significant element of the financial summaries section is the debt summary and analysis. Debt has a long-term impact on the budget because it commits current and future funds over the life of the debt instrument. Thus, information on both the short- and long-term implications of this indebtedness should be provided in the budget. In addition, information on current outstanding debt, future debt service requirements of current obligations, and analysis of current debt levels and legal debt limits should be provided.

The best budget documents include narratives along with tables to explain the significance of the financial summaries. Narratives should address significant financial trends, overall municipal financial condition, long-term budgetary impacts, and major shifts in budget priorities.

## Operating Detail

The budget operating detail is usually the longest section of the budget document. This section outlines the operational and spending plans for government agencies and programs. Information on the agency mission, staffing levels, performance objectives and indicators, expenditure levels, and possibly, financing sources is presented for each department or program.

**Objectives .** The budget's operating detail meets three important objectives:

- Allocate resources among departments and programs. Probably the most important function of the budget's operating detail is to show authorized spending levels for government departments and programs. The core of the operating detail is each agency's or program's spending plan.
- Establish performance objectives and measures. Another important function is to set performance objectives for departments and programs. These are specific objectives to be achieved during the budget period; they must be tied to the agency's mission and should describe the method to be used in measuring performance against the objectives.
- Report prior-year operating results and accomplishments. The operating detail should offer information on results and accomplishments of prior years. This is usually accomplished by listing expenditures and performance data for three successive budget years (e.g. prior year's actual, current year's estimates, and budget year's proposed). Some budgets also list the accomplishment by department or program during the prior year.

**Features .** Standard features of the operating detail include the following:

- Departmental/program mission statements.** A mission statement, describing functions and activities of each department or agency, should be included. Some budgets include mission statements for both departments and their sub-units (e.g. divisions, bureaus).
- Performance objectives and measures.** While the policy overview sets organization-wide budget goals, the operating detail section establishes specific performance objectives for departments and programs. These objectives detail what departments and programs expect to accomplish during the budget period. In the best budgets, objectives are tied directly to organization-wide goals.

Objectives should be specific, measurable, and sensible. For example, an objective for a housing program might be to privatize 200 housing units in the budget year. This objective is explicit about what is expected and what data must be collected to measure performance results. In this example, the objective is measured quantitatively by the number of units privatized within the budget year.

A performance objective may use a qualitative measure to explain how and why an objective was (or was not) achieved. In the above example, a reduction in the agency's ability to privatize the expected number of units could be due to redeployment of agency staff.

The measurement used in this example is an effectiveness measure. While a full discussion of various performance measures is beyond the scope of this paper, measurements commonly used include:

- *effectiveness* measures, which determine how well a program meets an objective or fulfills a need
- *efficiency* measures, which compare resources used with results obtained
- *demand* measures, which assess the severity of a problem or the scope of work to be performed
- *workload* measures, which indicate the amount of work that must be performed to accomplish a specific task.

One or more of these measures may be presented for each budget objective. Ideally, three years of data should be presented for each measure to allow for adequate comparison.

**•Financial data.** The heart of the operating detail section is the spending detail for departments and programs. As with performance data, three years of data (i.e. prior-year actual, current-year budget or estimated current-year actual, and proposed budget year) should ideally be presented.

The format for presenting financial data is guided by the overall budget format. If the budget is a line-item budget, the emphasis of the presentation will be on spending categories, or objects of expenditure, including: salaries and wages, fringe benefits, supplies and services, and equipment. If the budget is a program budget, the presentation will classify expenditures by program, not by objects of expenditure. This type of presentation may cut across departmental lines if more than one agency is involved in administering a major program. For example, "Public Safety" may include expenditures made by the police, fire, and public health departments. For the performance-based budget, unit costs and performance measures are provided for each program and activity.

**•Staffing and organizational structure.** The last major piece of information included within the operating detail is the level of authorized staff for departments and programs. Because personnel costs are a major portion of spending for most governments it is important to provide information on the number and type of positions assigned to specific functions.

There are many of ways to display staff information. The budget should include information on the number of full-time equivalent (FTE) positions assigned to a particular department, program, or activity. This approach avoids the problem of grouping full-time and part-time positions together, by converting part-time positions to full-time equivalents. Staffing information also may be summarized on a table elsewhere in the budget so that interdepartmental

comparisons can be made. Organizational information in the form of organizational charts also may be included at the departmental level.

**Suggestions for Preparing Operating Detail** . Because of its sheer volume, the operating detail takes the longest to prepare. Some suggestions for preparing operating detail are outlined below.

•**Determine level of detail.** How much information to include about each department or program is the main decision to be made in preparing this section. Several factors will determine how this basic question is answered:

- *Legal requirements.* These will dictate, in part, the level of the operating detail needed. Depending upon the type of government, central government laws or local ordinances may specify how much information is presented. The prior year's budget is the best guide on how to meet specific legal requirements.

- *Executive and legislative preferences.* The chief executive or administrator may prefer a certain level of budget detail because of its impact on budgetary decisions. The legislative or governing body may work out an agreement with the chief executive or administrator on the level of detail presented in the budget.

- *Placement of information.* Detailed budget information need not be presented exclusively in the operating detail. Instead, certain detailed information may be shown in summary tables. Government may also choose to exclude certain details from the budget document entirely and instead include them in supplemental documents made available to decision-makers upon request or as the need arises.

- *Type of document.* Another factor to be considered is the type of budget document being prepared. To facilitate budget deliberations, proposed or draft budgets must present more detailed information than do adopted budgets, which may only include summary data.

•**Design consistent formats.** Budget document users will find it much easier to comprehend financial and program data that is presented in a consistent format. Only one set of budget categories should be used for similar programs or fund types. Ease in reading and making comparisons between programs should naturally follow. Use the same format for program narrative and tables for similar departments and programs. The format selected also will determine what emphasis will be placed on data versus narrative. Some budgeteers may choose to make their points with data for ease of reading. Narrative may be used to emphasize priorities and link the chief administrator's priorities to the departmental objectives. Select an attractive, easy-to-read format. An attractive, clearly presented format will enhance the presentation of budget information. Liberal use of white space and headings can contribute to its readability.

•**Determine order of presentation.** The order in which departmental operating detail is presented may not seem like a major concern, but it does contribute to the utility of the budget document. A few simple guidelines can assist with this task. Present departments or programs

alphabetically. Department and budgets presented in alphabetical order make it easier for a reader to locate a particular budget. This also avoids the perception of showing preference to departments or programs presented at the beginning of the section. The policy overview and financial summaries should precede the operating detail, since the operating detail comprises the longest section of the budget and flows from organization-wide policies and finances.

•**Prepare tables and narrative.** Actual preparation of financial schedules or tables is made easier by keeping tables as simple as possible. Combine financial data with performance objectives and data only if it will not clutter the table.

Operating detail narrative may include mission statements, performance objectives, and possibly, a discussion of prior-year accomplishments. To the extent possible, narrative should be integrated with financial, performance, and personnel data to make for a more cohesive document. The success of the budget narrative will depend largely on clarity and persuasiveness.

## **The Final Document**

The budget document is the final product of a lengthy process. The budget's quality depends largely on the quality of that process. At each stage of development, the budget takes on a different form. Proposed budgets are usually the most comprehensive and largest versions because they contain critical decision-making information. The adopted or final budget, on the other hand, may be a smaller summary document used to communicate final policies and appropriations.

Regardless of form or size, budget documents have three purposes: (1) to integrate diverse, and sometimes competing, revenue-raising and spending proposals; (2) to encourage debate and thoughtful deliberations over important issues; and (3) to communicate budget decisions in an accurate and clear manner.

The budget is a decision-making document: it is the basis for important fiscal and policy decisions. An effective document encourages debate and proper consideration of budgetary issues by delineating the issues and informing participants on the implications of specific actions or inactions.

A useful budget document communicates budget decisions accurately and clearly. At different stages of development, the budget reflects decisions made by department heads, the chief executive or administrator, and finally, the governing body. The budget must accurately reflect the results of this process. The budget serves as the official action plan for managers and staff charged with carrying out government functions and programs.

The document should be printed and formatted in such a way as to enhance understanding and utility of the budget to the lay reader. It should be attractive, consistent, and oriented to the reader's needs. To this end, the budget document should include reader guides, budgets in brief, and graphics that will communicate these policies and priorities effectively. The budget should

be able to provide its audience with an understanding of the services being provided, the cost of these services, and the benefits to be obtained from providing these services.

No two budget documents are alike, even if they are prepared for the same local government. A number of factors contribute to such diversity and variation. Three of these factors are:

- Laws and traditions, which affect both the process and the budget document, vary considerably from country to country and from one jurisdiction to another.
- Turnover among administrators and elected officials, whose ideas and preferences influence the budget makeup, can alter the look of a budget.
- Budgeting remains more an art than a science, and like other works of art, the budget document is unique to the artist.

## **CLOSING THOUGHTS**

Each government is unique. Budget documents vary in size, format and length depending on the preference of the governing body or elected officials. In some cases, municipalities may have to develop both a control and a policy budget: the former to satisfy reporting requirements of the central government and the latter to satisfy the policymakers' desire to communicate to the public and business community what the municipality hopes to accomplish. Ultimately, the budget document is the vehicle for informing the public, the business and investment communities, the central government, and others regarding the community's investment policies and priorities.

## **CHAPTER 2**

### **FINANCIAL/BUDGET POLICIES AND PRIORITY SETTING**

#### **PURPOSE**

The purpose of this chapter is to enable you to:

- Understand the importance of having the Council establish policies and program priorities for the budget process
- Identify various ways that the process of policy and priority setting can be developed
- Learn how other municipalities have accomplished this process
- Participate in a priority setting process.

#### **HOW THIS CHAPTER WILL BENEFIT YOU**

All too often, the budget debate begins a couple of months before the new fiscal year and after the executive officer has submitted the proposed budget to the Council for consideration and approval. At this time, most decisions have been made and all the resources allocated. The complaint from Council members is universal. Council members say their priorities were not considered and that the budget is not responsive to the needs of the city or their community. There is usually some truth in what they say. What often results is a detailed scrutiny of the traditional line item budget as it has been presented to the Council. Haphazard suggestions are offered to reduce various line items to make up for the perceived budget shortcomings without any understanding of the impact of these suggestions on the organization. This reaction is rarely thought out and rarely pleases anyone. A better, more rational, and more focused process is needed.

This chapter and manual offer a different approach to traditional budgeting. Traditional budgeting is focused on control and purchases. Traditional budgeting entails a line item approach without much indication of what is to be done or achieved in the delivery of city services. Traditional budgeting does not concern itself with the budget as a policy document and therefore generally does not address financial policies and budget priorities. On the other hand, the program budgeting model suggests that one of the budget's purposes is to be a policy document, and therefore it should include financial or budget policies and program priorities as an integral part of it. These policies and priorities establish the framework and direction for the Council and city staff. This chapter will discuss budget policies and program priorities and show you how you can incorporate them into an expanded budget process.

## POLICIES AND PRIORITIES

Establishing financial (and budget) policies as well as program priorities is an essential part of a good budget process. These policies and priorities constitute the foundation upon which the budget is built and contribute to the effective management of the city's financial resources. They can also link past and future budgets with the current budget and disclose assumptions that are critical to understanding current budget decisions. Often these policies and priorities are assumed to be in place. However, a closer examination reveals that local governments have rarely formalized their policies and priorities in an ordinance or resolution or created a process to review them on a regular basis. Generally, officials cite national laws or practices that have been institutionalized over the years as their budget policies and program priorities. The statement "that's the way we have always done it" generally describes their policies and budget priorities. With increased responsibilities for service delivery being given to local governments, a more formal and explicit statement of financial policies and budget priorities is needed.

Financial policies are general principles that guide the financial management of the city. These principles provide the framework or set parameters in which routine financial decisions are made. They may also represent long-term financial goals for a government. A city's financial policies may not only include budget policies, but also more specific sections on the operating budget, capital and debt budget, as well as reserves, accounting, auditing, financial planning, and grants and trusts. The subjects included in a specific budget are largely left to the individual jurisdictions and will vary from one to the other depending upon their needs.

Financial policies have some common characteristics. They tend to:

- Be more general and long-term (than budget priorities)
- Change rarely
- Represent a framework in which routine financial decisions are made
- Be formally adopted by Council action
- Be reviewed periodically (every three to five years) to ensure that they are current.

For example, the City of Dallas<sup>1</sup> adopted its statement of financial management policies in 1978. The policies, referred to as *Financial Management Performance Criteria*, comprise a framework in which all of the City's financial decisions are made. In recent years some changes have been made to the criteria to accommodate new financial practices and techniques where there were no guidelines, but generally the criteria have not changed significantly in 18 years. Because the criteria were written and formally adopted by the Council, they demonstrate to the public, investors, and rating agencies (which evaluate the credit-worthiness of the City's municipal debt) the way that the City of Dallas will conduct its financial affairs now and in the

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Dallas, Texas, USA.

future. The criteria provide a foundation for managing Dallas's financial resources and a context for evaluating changes in the financial operation of the City. In part, the adoption and conservative construction of Dallas's statement of financial management has contributed to the City's strong financial condition and high credit rating for its municipal debt.

Exhibit 2-1 contains the City of Dallas's *Financial Management Performance Criteria*. The current status of the criteria is reported to the Council with the annual budget submission to show how the annual budget complies with the criteria. Clearly, any deviation from the criteria in the annual budget submission would be a policy issue of significant proportion and one that would be debated. Needless to say, that does not happen. Should there be a need to revise the criteria, that issue would be addressed in an *Issue Paper*, which will be discussed in a later chapter.

As mentioned previously, U.S. cities have considerable independence in developing financial policies because of the nature of the U.S. government system and emphasis upon local autonomy and self-rule. Exhibit 2-2 contains an extract of the fiscal policies from the City of Bozeman.<sup>2</sup> The fiscal policies of Bozeman include policies on the budget, as well as on revenues, expenditures, reserves, debt management, and accounting and financial reporting. Note that their budget policies (Exhibit 2-3) encompass both decision-making (e.g. maintenance and replacement of capital assets) as well as procedural policies (e.g. availability of the budget document) and also include a rationale for each item. The rationale helps explain why the policy is needed.

Financial policies, once adopted, benefit a city in a variety of ways. They can:

- Provide a framework in which financial decisions are made more routine
- Align Council and management and improve communication on financial management issues
- Help focus policy issue debates when anticipated actions indicate future violations of existing financial policies
- Provide a basis to periodically assess a city's financial status during the year (a new budget proposal).

Budget priorities, on the other hand, are more specific guidelines established by the Council for a fiscal year. These priorities could take several different forms. *Program priorities* are Council guidelines indicating that one program's budget needs to be increased more than others' by allocating additional funds or reallocating existing funds from other programs. For example, Council may indicate that street cleaning and repair programs should receive additional funding before park and median maintenance needs or that maintenance needs should be met before investing in new facilities. *Resource priorities* might favor use of fees and charges in lieu of general property taxes or might stipulate that any increase must be funded from cost reductions in other service areas. The purpose of establishing budget priorities before the budget itself is

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Bozeman, Montana, USA.

developed is to provide an agreed-upon direction in which the next year's budget will be developed.

Budget priorities naturally vary from jurisdiction to jurisdiction but have some common elements. Budget priorities tend to be:

- Short-term—usually one budget year
- Informally arrived at by the Council (through informal discussion or a straw poll)
- Changed more often than financial policies
- Reviewed and set annually.

Budget priorities tend to be less structured than financial policies but are no less important. Establishing a dialogue with the Council to arrive at budget priorities and guidelines can significantly improve the budget development process because this dialogue:

- Improves communication with the Council
- Eliminates surprises
- Involves the Council early in the process so their issues can be identified and worked in
- Focuses the attention of the budget debate upon the policy issue of whether the budget meets the program priorities and budget guidelines established
- Allows management to alert the Council to important upcoming issues in the budget.

Budget priorities and guidelines focus on the upcoming budget year. Even though they are short-term they can be drawn from a variety of sources. Some cities have extensive multi-year strategic planning or community planning processes in place. Taking into consideration the next year's priorities makes the development of program priorities relatively easy. Other cities may use Council retreats or workshops convened early in the year to discuss these issues, review the status of programs, and determine budget priorities. Still others may rely on informal discussions with individual Council members to determine their priorities. Regardless of the method used, the point is that determining budget priorities and guidelines early in the budget process is essential. Exhibit 2-4 provides an example of budget priorities and guidelines for the City of Lublin, and Exhibit 2-5 for the City of Krakow.

Adopting financial policies and setting budget priorities and guidelines are important first steps in the budget development process. Together they provide the framework and specific direction to build a budget that will meet the needs of the community and elected officials.

## PRIORITIZING TECHNIQUE

In a group process, how often does the person who speaks the most, has the most authority, or is the most emotional usually get his/her way regardless of how the other group members might feel about an issue? This situation often creates a feeling among group members that “their” issues will never be addressed. This can lead to a lack of commitment to resolve the issue selected and usually results in working first on an issue that may not be the most crucial. What is needed is a systematic way to select the issue that is the highest priority for the group. This section will acquaint you with the *nominal group technique*, which tries to give everyone in the group an equal voice in issue or program prioritizing. The steps in the process are as follow:

- Have each member of the work group (Council) write or say the issue or program that he/she thinks is the most important.
- Collect the responses and record them on a blackboard or chart paper.
- Consolidate the responses where there are similar issues or programs so that they are not duplicated.
- Ask the work group to list on a separate piece of paper the letters corresponding to the number of issue statements the work group produced. For example, if a group of 15 produced 10 programs or issues, then they would list A-J on their paper.
- Make sure the master list of programs or issues has letters, too. Ask the work group members to prioritize the issues. For the most important issue, they should write “10” next to the letter, “9” for the next most important, etc. For example, the problem list might look like this for the first five items for one person:

A. Cleaning the streets	10	
B. Picking up the garbage	7	
C. Maintaining the parks		3
D. Providing public lighting	5	
E. Rebuilding the city's infrastructure	8	

- Have each participant rank the issues from 10 (the highest) to 1 (the lowest) on his/her paper and report the ranking from A-J.
- Add up the ranking for each issue. The issue with the highest number is the one most important to the work group.
- The result is a listing of the group's priorities.

Note: If there are many issues to be considered, an alternative method is needed that limits the number of issues by applying the rule of “one half plus one.” Under this rule, you rank only one half of the items plus one. For example, if 30 issues were generated, the work group would rank only 16 of them.

## **PRACTICE EXERCISE**

You are asked to write what you think is the most important problem confronting your city in the next budget year and share it with the group. The instructor will use the nominal group technique to determine the relative priority of the group’s issue statements. The group will discuss the merits of this type of prioritizing exercise from the participants’ perspective and relate it to working with Council members.

## CHAPTER 3

# PREPARING A BUDGET CALENDAR

### PURPOSE

The purpose of this chapter is to enable you to:

- Identify the five phases of the budget cycle
- Know what a budget calendar is and what it includes
- Describe the benefits of preparing a budget calendar
- Prepare a budget calendar for your jurisdiction.

### HOW THIS CHAPTER WILL BENEFIT YOU

In this chapter, you will receive an overview of the process by which a budget is prepared for local governments. While each city in Poland must comply with certain legal requirements, formats, and dates, the process can be supplemented to improve the planning process and input to the budget to better reflect the needs of the community and local government. The process outlined here uses the expanded *program budget model calendar* to illustrate changes from the traditional budget calendar. An expanded budget calendar will:

- Increase the amount of time allocated to the beginning of the budget preparation process for planning the budget and analyzing budget requests in order to reduce time pressure involved in developing the budget
- Involve the Council and citizens early in the budget preparation process so that budget policies and priorities can be set and attention focused on key decisions
- Give departments early direction on Council priorities.

### BUDGET CYCLE

Public officials (Council) and government managers need to be familiar with the process of developing budgets to administer an efficient local government. In addition, they must be ready to participate in these processes by preparing and presenting their own department budget or the budget of the entire city to the Council. They must take into account not only their own financial and management perspective, but also overall considerations such as political, social, and economic issues affecting the community.

The budget process can be divided into five phases or steps in the process, usually termed the “budget cycle.” These phases are planning, preparation, adoption, execution, and audit.

## **Planning**

This is the important first step. The Mayor or City Manager is responsible for planning the budget cycle. Ideally, the planning phase would include: (1) adopting financial policies (if not already completed), (2) establishing Council priorities, (3) developing a budget calendar with key dates in the process in which the Council wishes to participate, and (4) providing a systematic process to review issues and policies that need to be addressed in next year’s budget.

## **Preparation**

Departments prepare budget requests based on guidelines and instructions provided by the Mayor, City Manager, or Budget Director. Once submitted, the executive officer and budget staff review and adjust the budget to reflect available resources, new policies and programs, and other high priorities. The result of this balancing act is a recommended budget.

## **Review and Adoption**

Once the budget is recommended by the executive officer, the Council’s role is to review it, hold legally required public hearings, modify the budget to reflect needs that have not been addressed, and vote to adopt or reject the budget effective at the beginning of the fiscal year. The budget becomes a legally binding document only upon passage by the legislative body (Council).

## **Execution**

After the adoption of the budget by the Council, the next step is the execution of the budget or the implementation by the executive officer and the city staff. The ideal budget represents a policy document, a financial plan, an operations plan, and a communication device incorporated into one document. Now the job of the executive officer is to put those multiple plans into action within the resources given. Since the budget document is a plan and based upon estimates, close monitoring is needed to ensure that the anticipated revenues are received and expenditures stay within the limits imposed by the Council. Generally, the chief executive officer or budget officer will control the use of these funds through a trimester allotment process.

## **Audit**

This is the final step in the budget process. It provides a way to check the budget execution phase to ensure that it was handled honestly and within the budget and legal requirements.

## BUDGET CALENDAR

One of the first steps in planning a budget is preparing a budget calendar. The budget calendar identifies the dates by which the city needs to accomplish activities to produce a budget for submission to the Council by the legally required due date. Generally, the budget officer, working closely with the executive officer, prepares the calendar. The budget calendar must take into account the start of the fiscal year, the legal budget submission and public hearing requirements, publication dates for public reading of the budget ordinance, dates for reporting the budget to the central government, and other considerations of the Mayor and the Council.

A budget calendar has many benefits. It organizes the entire budget process from beginning to end. It identifies critical milestones and budget deadlines that must be met. It helps show the public and other external agencies the process used to prepare the budget and the ways in which they can have input. It provides a means to open the budget process to the public. The planning, preparation, adoption, and execution phases of the budget process typically involve the year round effort of many city staff at all levels in the organization. The staff are involved in identifying service needs, developing strategies for meeting those needs, and developing detailed revenue and expenditure plans to execute strategic plans. The budget calendar allows them to see the big picture and their role in that process.

The budget calendar contains specific activities that generally will be required by all jurisdictions at some time in the process. These include:

- Making preliminary revenue estimates
- Preparing and distributing instructions and forms
- Receiving completed budget request forms
- Analyzing budget requests (central budget office)
- Completing the budget review and making final budget decisions (executive officer)
- Submitting the recommended budget to the Council
- Conducting public hearings
- Reviewing and determining the Council's changes (if any) to the recommended budget
- Adopting the final budget ordinance (Council)
- Approving or vetoing the adopted budget (executive officer)
- Completing administrative and financial transactions for finalizing budget appropriations
- Specifying the commencement of the fiscal year.

## HOW TO MAKE A BUDGET CALENDAR

Making a budget calendar is relatively simple if you observe the following:

- Start with the end date in mind (beginning of the new fiscal year) and work backward
- Add the legal requirements
- Add public hearing and publication requirements
- Leave sufficient preparation time between the final decisions of the executive officer and the submission of the budget to the Council in order to produce a quality product
- Add other key activities and dates leaving enough time for adequate preparation and review
- Review prior year budget calendars and adjust where needed to improve the process
- Coordinate the preliminary calendar with the executive officer
- Adjust schedules accordingly
- Finalize the budget calendar.

## EXAMPLES

Budget calendars may vary significantly depending upon local requirements and the level of detail they include. Deadlines are a key element in any calendar. Exhibit 3-1 at the end of this chapter shows an example of a budget calendar developed by the City of Krakow for the 1996 budget.

A sample budget calendar is shown as Exhibit 3-2. For comparative purposes, an example of a budget calendar from a U.S. county is included in Exhibit 3-3.

## PRACTICAL EXERCISE

To give you a better awareness of the budget calendar development process, a simple exercise has been designed to give you experience in this area. Using your own city as a model, prepare a one to two page detailed budget calendar with dates, major activities, and responsible persons for each activity. Be prepared to present your calendar to the group.

**Exhibit 3-1**  
**City of Krakow**  
**Sample Budget Calendar**

**Exhibit 3-2**  
**Sample Budget Calendar**  
**Adoption by December 31**

**Exhibit 3-2**  
**Sample Budget Calendar**  
**Adoption by December 31**

July 15      Budget office makes first estimates of revenues, inflation, central grants, subsidies, and tax rate maximums.

July 20      Council holds public hearing for citizen input.

August 1     Council passes resolution on budget policies and priorities.

August 15   Budget office distributes budget instructions and forms to departments; provides departments with uniform assumptions as basis for their budget requests.

September   Departments submit budget request to budget office for review and analysis (Discussions with departments—revision of requests).

October 10   Budget office revises estimates of revenues, inflation, central grants, subsidies, and tax rate maximums.

October      Mayor reviews budget office recommendation with Treasurer and budget staff.

Nov. 1-5     Department appeals; final city board decision made. Print board's recommended budget and distribute to public, press, and Council.

November 15              Council budget commission holds public hearing on city board's proposal, begins review of board's proposal.

December 1   Final Budget office revision of estimates of revenues, inflation, central grants, subsidies, and tax rate maximums.

Dec. 10-15   Adopt budget. Set property tax rates, rents, user fees (for transportation, water, sewer, and garbage collection).

March 31     Adjust budget based on final central government factors.  
(Next Year)

**Exhibit 3-3**  
**U.S. County**  
**Sample Budget Calendar**

**Exhibit 2-1**  
**City of Dallas**  
**Financial Management Performance Criteria**

**Exhibit 2-2**  
**City of Bozeman, Montana**  
**Fiscal Policy Extract**

**Exhibit 2-3**  
**City of Bozeman, Montana**  
**Budget Policy Direction**  
**[extract]**

**Exhibit 2-4**  
**City of Lublin, Poland**  
**Budget Priorities and Guidelines**

**Exhibit 2-5**  
**City of Krakow, Poland**  
**Budget Priorities and Guidelines**

## **CHAPTER 4**

# **CITIZEN PARTICIPATION IN THE BUDGET PROCESS**

## **PURPOSE**

The purpose of this chapter is to enable you to:

- Understand the need for local governments to involve citizens in the decision-making process
- Identify techniques to increase citizen participation in the budget process
- Identify the advantages and disadvantages of various citizen participation techniques.

## **HOW THIS CHAPTER WILL BENEFIT YOU**

Changes occurring in local governments require increased citizen involvement in local government decision-making. These changes are pressuring local governments to conduct city business, provide services, and communicate with citizens differently than in the past. This chapter will describe the new environment in which local governments work and how interaction with citizens can be incorporated into the budget process. Interaction will take different forms and potentially produce differing results.

## **NEW ENVIRONMENT**

The transition from state socialism in the Newly Independent States and Central and Eastern Europe has created an opportunity for new political, economic, and social structures. Reformed governments, economies, and social institutions have directly impacted local governments as new powers and responsibilities have been devolved. Local governments must assume these responsibilities quickly and manage the resources that have been entrusted to them as efficiently and effectively as possible for the benefit of their citizens.

Citizens play a crucial role in a democratic government system. Through free elections, citizens select the government leaders at the national, regional, and local levels. These leaders in turn

make decisions on behalf of the citizens and are accountable to them. Within the democratic system, citizen involvement in the governing process is paramount because governments rule only with the consent of the governed. Leaders who choose to ignore the citizenry may soon find themselves voted out of office.

Under the system of local government democracy established in Poland in 1990, citizens are free to vote out city councils and city administrations that do not respond to the needs of the citizenry. To avoid the potential for turnover, elected officials need to recognize the new power that resides with the citizenry and create the means to involve citizens in a dialogue with the government over issues in which they both have a vested interest. The development of the annual budget, which establishes the priorities and funding for a given period, is an important event that requires public input early in the process. No longer are budgets conceived in an office in the capital and passed down to the gmina for local citizens to accept. No longer is the budget process closed to citizens. The process now springs from the citizenry, and the role of governments is to meet the citizens' needs. A citizen participation process that responds to this new environment is essential.

## **CITIZEN PARTICIPATION TECHNIQUES**

Five citizen participation techniques used in the budget process will be discussed in this chapter:

- Formal budget hearings
- Town hall meetings in the community
- Citizen opinion surveys
- Focus groups
- Committees or task forces.

## **Formal Budget Hearings**

Formal hearings are the most common means for local governments to solicit public input to any significant government decision that will affect citizens. In many cases, formal public hearings may be a legal requirement. Some examples of hearings include zoning and land use decisions or annual budget decisions. Formal budget hearings are normally held after the budget is presented by the executive officer to the Council, which is during the period when the Council considers the budget. Public notices are published in a local newspaper announcing the date, time, and location that budget hearings will be held by the Council. Notices encourage citizens to come to City Hall to voice their opinion. This process will usually attract a few citizen speakers and meet the legal requirement to hold a public hearing, but generally does not produce effective input to the budget.

To improve the formal budget hearing process, local governments have tried other tactics. One jurisdiction tried to maximize citizen input by providing two formal budget hearings during regular Council meetings at the very beginning of the budget process, i.e. six to nine months before the budget was presented to the Council. In this manner, the public is notified that a budget will be developed, and organizations and individuals are invited to participate in the process. The additional lead time allows Council and staff to research and address issues presented and develop policies that reflect citizen interest and can be considered for funding in the subsequent year's budget. The public is involved at the beginning of the process rather than at the end after all the decisions have been made.

The cities of Krakow and Lublin have not established a formal hearing in their budget process. They do, however, permit citizens to address the Council on budget and other issues throughout the year at regularly scheduled citizen forums during City Council meetings.

While formal budget hearings satisfy the legal requirement to hold such hearings and are inexpensive, they are generally the least effective technique—especially if they are held after the budget is presented to the Council for approval, because citizen input cannot then be easily incorporated.

## **Town Hall Meetings**

A variation of the formal public hearing is the town hall meeting, which essentially serves the same purpose as a formal hearing—to solicit citizen input—but is more informal. Town hall meetings are held in neighborhoods at dates, times, and locations that are convenient for citizens. Evening meetings are common. Sometimes dates and times are negotiated with neighborhood associations to maximize attendance and comments at the meetings. The agenda is singularly focused on the budget, and the comment session is preceded by a city staff briefing on the budget to provide a common informational basis for citizens in attendance. Members of the budget staff and other service departments take part in the session to answer questions and take notes for future budget preparations. Elected representatives are usually present and moderate the discussion.

The same town hall meeting technique is used again by elected Council members after they receive the proposed annual budget from the executive officer. It provides the Council with one more opportunity to review the city's proposed financing plan with the citizenry before the budget is adopted for the next fiscal year.

Because town hall meetings are informal, closer to the public, and more focused on the budget, they tend to provide a broader and more effective mechanism for including public input in the budget. Town hall meetings promote empowerment of citizen groups. They allow staff an opportunity to answer questions and resolve problems before a formal hearing and action by the Council. The logistics of setting up and conducting public meetings outside City Hall and the usual need to hold multiple meetings in different parts of the community may be viewed as disadvantages to this technique. However, from a different perspective these obstacles can be viewed positively. If the bureaucracy is seen as generally being out of touch with the citizenry, holding town hall meetings can be a perfect opportunity for the local government to get out in the community and demonstrate its commitment.

## **Citizen Opinion Surveys**

Citizen opinion surveys are a technique used by municipalities to more accurately gauge public opinion on the quality and quantity of city services. A questionnaire is designed and posed to a representative sample of citizens. Usually a private firm is engaged to assist the city in preparing the questionnaire, conducting the survey, and evaluating the results. Surveys can be conducted by telephone, in person, or by mail. The more personal the survey methodology, the more expensive, but hopefully the more accurate as well. The results are used to determine the citizens' priorities for services, to evaluate existing services, and to investigate citizens' willingness to support tax increases. By conducting surveys on a recurring basis (every two to three years) using similar questions, the city can determine changes in public opinion and whether actions taken by the city in the interim have been effective in influencing public opinion.

The City of Krakow has experimented with citizen opinion surveys. In 1993, the city faced two issues related to citizen involvement: advertised meetings resulted in little turnout, and many of the government programs offered by the previous system bore no relationship to customer demand. The solution was to design and conduct an opinion survey to determine citizen interest on specific city issues. The City and the long-term advisor designed a telephone survey similar to ones used by several U.S. cities. In January 1994, they contacted 287 households by telephone. The survey focused on the 14 largest programs and asked the community: (1) satisfaction with service provided, (2) desire for increases or decreases in service levels, and (3) willingness to pay more taxes or charges for program increases. The intent was to establish a link between service level and customer demand. The survey also asked the public's opinion on the priorities of programs and some of the more politically difficult issues in the budget.

The survey revealed some interesting insights into public opinion and provided objective information about citizens' opinion of city services. For example:

- The program with the highest community satisfaction was Culture (77 percent) followed by Primary Education (72 percent) and Central Heating (60 percent). The lowest scoring programs were Streets (19 percent) and Financial Assistance to the Needy (25 percent—many thought this program should improve its means testing), and Water and Sewer (34 percent).
- Sixty-four percent supported service increases in Water and Sewer; 58 percent in Solid Waste, 57 percent in Streets, and 54 percent in Parks. However, only in Primary Education, Water and Sewer, and Parks were the majority of supporters willing to pay more.
- Eighty percent supported the City Board's top priorities of Streets, Housing, and Schools.

- On issues that were politically difficult, 81 percent believed that the City should contract out programs to reduce costs, and 97 percent believed that utility rates should be based on actual use, rather than everyone paying the same rate.

Citizen opinion surveys can provide valuable, objective information about the public's perception of service quality and service priorities. This information can be very useful to influence decision-makers in developing program priorities for the budget. Surveys tend to be expensive both in staff time and financial cost; however, they produce more objective findings to guide decisions affecting the budget and city services.

### **Focus Group Interviews**

Another technique used to gauge citizen opinion is the focus group interview. The focus group technique has been borrowed from market research conducted by private business. The objective of the focus group interview is to determine why customers might or might not buy a product or participate in a service the city offers. This technique might be useful for municipalities when marketing a new product or service, such as recycling, or when making substantial changes to an existing service.

A focus group includes approximately ten people, representing a cross-section of the intended customers. People are selected knowing that they will be learning about a new service that the city is considering. The group is then asked questions in an objective manner about the proposed service. The session is either recorded by audio tape or with extensive written notes to accurately capture the proceedings so that the information can be analyzed later. The focus group interview is repeated three or four times with different groups to gather comparative information.

Focus group interviews can provide valuable information about a specific service from a group of potential customers that a city may expect to serve. This technique can produce very good results provided that the right questions are asked and that the group is representative of the intended customer base. The fact that the focus group interview is usually focused on a single service may limit its use to broader budget or city-wide service policy decisions.

## **Citizen Committees or Task Forces**

Another technique used to solicit citizens' involvement in the decision-making process of local government is using business, community, or service agency leaders to advise local governments on budgeting, financial forecasting, or other methods of increasing efficiency and effectiveness. Asking citizens to serve on a citizen committee or task force to review the budget and funding levels has several benefits. First, these citizens bring their own private business or service agency experience to the local government. Secondly, involving them in the process tends to improve communication between the city, elected officials, and community leaders. As the budget is developed and reviewed by an increasing number of diverse interest groups and people, these key leaders can be influential when the Council is faced with critical decisions.

For example, one municipality put the citizen committee technique to good use in planning for capital improvements. The Mayor and City Council appointed 100 citizens to a citizen's committee to develop a capital improvements program. The committee was divided into four sub-committees to address drainage, transportation, parks, and public safety issues. These committees met over a three month period, conducting field trips, debating needs, and setting priorities. In the end, their recommendations for the final capital improvements program were substantially smaller than the estimates of city staff.

The preliminary work done by the committee made the task of the City Council much easier. In the next round of reviews, a select Steering Committee made up of the sub-committee chairs worked with the City Council to pare the program further. When the program was adopted by the Council, the Steering Committee formed a Citizen Committee for City Bonds to sell the program to the voters.<sup>3</sup> The Citizen Committee for City Bonds involved almost all of the members who had worked on the capital improvements program development in the campaign to support the bond referendum. Each member of the committee contacted ten families to encourage voting to support the bonds. In addition, the committee members conducted town hall meetings and spoke at service clubs. They also conducted brown bag lunches with City employees, developed an election brochure to educate and attract voters, and created a telephone hot-line to respond to citizen questions. News releases and access television were also used to publicize the issues.

In addition, the citizen committee played a significant role in fund raising. Their efforts were responsible for successfully raising private donations in the community to fund a telephone bank, signs, brochures, postage, advertising for early voting, the contacting of ten families per

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Note: General Obligation bond programs customarily have to be approved by a majority of the voters in an election before the city can issue municipal bonds.

member, and the soliciting of endorsements for the bond package by business groups, economic development agencies, and other associations. The result of this citizen effort was that early voting was over 150 percent, and the total voter turnout was three times that of the previous bond election. All issues passed on an average of four to one.

## EXAMPLES

The ICMA book *How Effective Are Your Community Services*<sup>4</sup> contains several public opinion survey instruments in an appendix. An illustrative questionnaire for a household park and recreation survey is included as Exhibit 4-1.

## PRACTICAL EXERCISE

The group will break into five smaller groups of approximately equal size. Each group will be assigned a specific citizen participation technique. The groups are assigned to brainstorm ways to maximize the advantages of the specific citizen participation technique and to minimize its inherent disadvantages. Comments from each participant should be written on chart paper under the specific pros and cons of each technique. The group should select what they believe are the best ideas from each resulting list. Each group will select a spokesperson who will report their group's consensus list at the end of a set time (15 minutes).

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Harry P. Hatry, et al. *How Effective Are Your Community Services*, Procedures for Measuring Their Quality, second edition. Washington, D.C.: Urban Institute and ICMA, 1992.

**Exhibit 4-1**  
**Citizen Opinion Survey, Park and Recreation**  
**Source: *How Effective Are Your Community Services***

## **CHAPTER 5**

### **PREPARING AND PRESENTING ISSUE PAPERS**

#### **PURPOSE**

The purpose of this chapter is to enable you to:

- Understand the value of a separate process to analyze, discuss, and decide policy issues and/or budget priorities at the beginning of the budget process
- Describe the steps to organize an issue paper process
- Delineate the benefits and costs of an issue paper process.

#### **HOW THIS CHAPTER WILL BENEFIT YOU**

In this chapter you will learn how an issue paper process can help clarify the budget process. Currently in Poland, the budget process is concentrated in the last three or four months of the calendar year. The process is usually labor intensive and time consuming. Insufficient time is devoted to improving the management of local resources, analyzing policy or service alternatives, or seeking new funding sources. The current system was adequate when budgeting was no more than an accounting tool and a mechanism to control revenues and expenditures for the central government.

Since 1990, increased responsibility for service delivery has been thrust upon local governments from the central government. Local governments have been given new powers and responsibilities to set local policies and to adopt budgets that support them. However, these changes are being superimposed on existing budget processes and time schedules that are inadequate. To deal with these new and increased responsibilities and powers, a revised process and schedule is needed. Local elected officials and city staff should be given more time to consider and decide important policy issues at a time apart from the annual budget process. With the increasing complexity of local issues, it is impossible to manage both processes well simultaneously. Currently there is no forum or process for dealing with policy issues except at budget time. This chapter offers you an alternative process that will increase the time and order of the budget process, improving both policy-making and budget preparation. You will also

learn the steps necessary to establish an issue paper process and know what costs and benefits can be expected.

## ISSUE PAPER PROCESS

An issue paper is a written document that addresses a specific local government policy or budget issue. The purpose of an issue paper is to provide elected officials with sufficient information (i.e. background, current situation, options, and analysis of options) and a recommendation on a specific issue, so they can make an informed policy decision.

The issue paper process described herein intentionally separates the policy decision-making process from the budgeting process. Separating the two provides time for policy issues to be discussed, deliberated, and decided, without having the pressure of budget deadlines looming. Once the policy decision is made, the budget decision is almost non-eventful since it has been agreed to previously. The budget process of funding these new policies and programs becomes an issue the Council is already aware of at budget time.

The steps in the issue paper process are:

- Identify issues.** Within a month after the fiscal year close, the chief executive officer and department directors identify and list potential issue paper subjects. From this list, the departments prepare a brief description (three or four sentences) about each issue.
- Determine priorities.** At a Council planning workshop, the chief executive officer shares and reviews the list with the Council, which augments it and prioritizes the issues that are considered important for further analysis and discussion prior to the next year's budget process.
- Organize the process.** The chief executive officer organizes the agreed upon issue papers into a presentation schedule and prepares instructions for the departments to follow in preparing and presenting the papers. Exhibit 5-1 and Exhibit 5-2 contain outline formats for budget issue papers and policy issue papers used by other cities.
- Prepare and present the issue paper.** Department directors prepare the issue papers based on the directions and sample outline format provided by city management. When the papers are completed, department directors brief the city management and present the papers to the Council. Copies of the issue papers are sent to Council members prior to the presentations so that they have sufficient time to read them. All-day workshops are planned for the formal presentations.

•**Receive Council direction.** After the Council has reviewed and discussed the recommendations, city management is advised what policy the Council wishes to pursue on specific issues and how the policy will be funded.

•**Implement decision.** Department directors and the chief executive officer develop the service plans and funding necessary to implement the policy decisions and incorporate them into the proposed budget for the subsequent year.

## **BENEFITS AND COSTS**

It is obvious that the issue paper process will provide more time to deal with policy formulation apart from the pressure of budget deadlines. The separation of policy formulation from the funding process also has other benefits including:

- Reduction of pressure on elected officials and staff at budget time because many difficult policy decisions have been decided
- Improved communication with the Council because it has been involved in making key policy decisions that are now included in the budget
- Enhanced budget quality because policy issues are linked with budget proposals.

In contrast, there are costs that will be incurred to facilitate the process. A separate issues development and analysis process requires staff with the knowledge and skills to identify and analyze issues and to determine alternative policies and funding sources. If staff with these skills are not available, they will have to be hired or trained. Additionally, the issue paper process extends the budget timetable because it is one of the first budget planning steps. The process may redirect resources from other activities normally accomplished during this period, which may cause other service disruptions if not carefully managed. Furthermore, the process will take more Council and staff time for workshop planning and preparation as well as briefings for issue paper presentations and discussion.

**Exhibit 5-1**  
**Budget Issue Paper Format**

**Exhibit 5-1**  
**Budget Issue Paper Format**

I. Executive Summary

II. Issues

III. Background

IV. Description and Analysis of Current Situation

V. Budget Options

VI. Analysis of Options

VII. Recommendations

**Exhibit 5-2**  
**Policy Issue Paper Format**

**Exhibit 5-2**  
**Policy Issue Paper Format**

- I. Executive Summary (2 pages minimum)
- II. Statement of Issues
- III. Background, Historical Trends
- IV. Description and Analysis of Current Situation
- V. Policy Options to be Analyzed
- VI. Analysis of Policy Options, Advantages and Disadvantages, Costs, and Benefits of Each Option
- VII. Recommendations

## **CHAPTER 6**

# **FORECASTING REVENUES AND EXPENDITURES**

### **PURPOSE**

The purpose of this chapter is to enable you to:

- Understand the importance of forecasting
- Identify the uses of forecasting in budgeting
- Identify and describe the tools and techniques employed in forecasting
- Employ these tools and techniques to improve your forecasting capabilities.

### **HOW THIS CHAPTER WILL BENEFIT YOU**

Budgeting is the craft of allocating scarce resources to benefit the many. Preceding chapters on budget planning have emphasized the need for financial policies, which provide a framework in which routine budget decisions are made, and budget priorities, which specify how the Council wishes scarce resources to be allocated to meet public needs. This chapter will add one more dimension to the planning process—forecasting.

Forecasting in local governments is an important management tool and guide for Council and management to anticipate and plan for potentially adverse financial events. During budget planning, forecasting can help shape the Council's understanding of the financial limitations under which the next year's budget will be developed. Annual forecasts of revenues and expenditures are the basis of the adopted budget. Once the budget is adopted and implemented, forecasts are made throughout the year to project revenue collections and program expenditures to year-end to ensure a balanced budget and to avoid a deficit. Clearly, forecasting plays an important role in budgeting from beginning to end. This chapter reviews the uses of forecasting. The tools and techniques employed in forecasting are discussed and are applied in a practical exercise at the end of the chapter.

## **USES OF FORECASTS**

Forecasting is the process of determining what a future situation will be given certain assumptions. In local government budgeting, forecasting is indispensable. Increasingly, local budgets are tied to the national economy and experience the same changes in the economic cycle. The most frequent uses of forecasts can be classified based on the length of forecasts: short-range (up to one year), medium-range (2-5 years), and long-range (6-20 years). For annual budgeting, short- and medium-range forecasting are more useful and relevant than long-range forecasting and will be the focus of this section.

### **Short-Range Forecasting**

Short-range forecasts cover a period of up to one year. The principal uses of short-range forecasts are related to the development of the operating budget and cash management. In developing the operating budget, annual forecasts of revenues and expenditures are needed for the next year's budget. These forecasts may occur at different times. Initial estimates of the next year's revenues and expenditures are used for setting priorities and budget guidelines. These estimates are continually updated and ultimately included in the budget. In cash management, forecasts of monthly cash inflows and outflows are used during budget development to project interest earnings on available bank balances. They are also done to identify the potential for monthly cash shortfalls and the need for interim financing during these periods.

Another use of short-range forecasting is for monitoring budget implementation. It is prudent to monitor the budget after adoption to forecast the actual performance of revenues and expenditures. If significant variations from budget are forecast based upon actual operating results, swift management actions may be needed to bring the budget back into balance.

Short-term forecasting helps management prepare a budget for the following year based on reasonable assumptions. By identifying variances from expected performance early in the fiscal year, short-term forecasting provides time for management action rather than crisis management. Finally, short-term forecasting is a tool for monitoring the budget and ensuring compliance with legal appropriations. When problems are identified, corrective actions can be initiated to eliminate them.

### **Medium-Range Forecasting**

Medium-range forecasts cover the period 2-5 years into the future. The principal uses of medium-range forecasts are for budgeting, policy analysis, and legislation. In budgeting, forecasting is principally used to project gaps between anticipated revenues and expenditures during the next 2-5 years. This prompts policy decisions to close these gaps. If decisions are implemented, the actual revenues and expenditures will not be the same, and the forecast gap will not be the same. The altered level will be the result of actions taken in response to the forecast.

Forecasting is also used to aid policy analysis. For example, wage negotiations in a multi-year contract will have fiscal implications beyond the current year. Identifying the future years' impact of these negotiations is critical for policy decision-making today. Decisions regarding funding capital improvements from own-source revenues reduce the availability of funds for operating expenditures and increase operating costs when the facilities are completed. These impacts are important elements in making capital improvement project decisions. Issuing debt to finance new capital facilities, likewise, has multi-year implications both in long-term funding of debt service and in operating the facilities when they are complete. Each of these factors needs to be considered with the multi-year impact identified at the time decisions are made. Once the decision is made, the financial impact is included in the medium-range forecast.

Medium-range forecasts are useful in determining the fiscal impact of legislation, especially tax or revenue legislation. For example, changing an allocation formula for sharing revenues with local governments will have multi-year impacts. Forecasting the multi-year cost impacts of this change in the law upon local governments and presenting this information to the legislative body is one way to forestall or reduce the adverse impacts upon the jurisdiction.

Medium-range financial forecasts help management and policy-makers to identify financial trends that will require management/Council action to avoid potentially disastrous financial results. Being prepared eliminates surprises and reduces management by crisis. Forecasts also promote more efficient operations of local government.

## **METHODS OF FORECASTING**

This section will focus on methods of forecasting revenues and expenditures 2-5 years into the future. Four general methods will be discussed, varying from the simple to the complex.

### **Best Judgment or Expert Method**

The "best judgment" method relies upon a person or "expert" to forecast revenues or expenditures. There is no single technique employed in this type of forecasting, which primarily depends upon the forecaster's subjective feelings, long-term experience, expertise, and familiarity with revenue or expenditure patterns. The key ingredient in this method is finding the "expert." Long-time budget officers or treasurers often act as the forecasting "expert" in a city.

The "expert" or best judgment method may produce reasonably accurate forecasts. It is also relatively inexpensive. One of the drawbacks of the method is that the lack of a standard technique makes it difficult to determine what was right or wrong with the forecast analysis. The method is also dependent upon a single individual, and a jurisdiction's effectiveness may be hampered if that person leaves.

## Trend Line Techniques

The trend line techniques rely entirely upon the year-to-year change of prior levels of a variable (i.e. a revenue source or expenditure) to forecast future years' revenues or expenditures. By determining the changes in the recent past, certain revenues and expenditures can be projected quite accurately into the future.

A review of the year-to-year change of a variable (revenue source or expenditure) can produce different conclusions about the type of change that has occurred and how that information will be used for projections. There are three possibilities: if a variable did not change in the past, the variable may be assumed not to change in the projection period; if the variable increased by a constant amount each year in the past, it is reasonable to assume that it will increase each year by the same absolute amount from prior years; and if the variable increased each year by approximately the same percentage, then that percentage rate of increase (or decrease) may be used as a constant growth rate in the future as it has been used in the past. For example, if a revenue source increased 9 percent each year for the last five years, one can assume that next year's increase will be approximately 9 percent. Note that trend lines assume that the past is a good predictor of the future. Unfortunately, that is not always true.

To enhance the usefulness of this technique, the following should be considered:

- The accuracy of the trend line forecast will improve when a longer history of the revenue or expenditure is used. Generally, forecasters rely on the most recent five annual increments of a revenue source or expenditure for forecasting, but a six to ten year base is not uncommon and enhances the reliability of projections based on the trend line.
- One-time occurrences should be identified and removed from the variable to avoid skewing the results.
- Trend line forecasts are most reliable for revenues not sensitive to economic conditions.
- Trend line techniques are not good predictors of turning points for a variable.

To determine the percentage rate of change or growth rate of a variable (revenue or expenditure) between time periods, use the following formula:

$$g_t = \frac{(V_t - V_{t-1})}{(V_{t-1})} * 100$$

where  $g$  equals the percentage growth rate of a variable,  $V$  is the variable, and  $t$  is the period of time.

To use the growth rate to project the next period's revenue or expenditure, multiply the latest period amount by the growth rate, dividing by 100, add 1.00, and multiply that sum by the latest period amount to arrive at the next period's projected revenue or expenditure. Repeat the process for the next period.

## Deterministic Techniques

Deterministic techniques use other factors than time in “determining” projections. The most common deterministic techniques rely on pre-established formulae in calculating a projected revenue or expenditure. For example, to calculate a license fee revenue, the forecaster estimates the number of licenses to be issued for a year based on historical records and multiplies that figure times the applicable fee for each license. The result is the projected revenue for that source.

Deterministic techniques can also be used for projecting expenditures. For example, to estimate the cost of staffing a new facility, the following should be considered: the estimated number of persons to be hired based on other comparable facilities, the average salary for full-time equivalent (FTE) position at a comparable facility, and the portion of the year that the facility will be in use in its first year. Taking the number of positions times the average salary per FTE times the fraction of the year the facility will be open will produce a projection of the staffing cost for the opening year of operation. Subsequent years' costs will be based on a full year's staffing.

Deterministic techniques are relatively simple, depend on a few assumptions, and are based on past

## Econometric Forecasting

Econometric forecasting combines economic principles with statistical theories. Econometric models permit the forecaster to consider the effects of several variables on a revenue or expenditure. The objective is to identify the independent variables, such as disposable income, population, prices, or inflation, that provide the “best fit” to project future changes in revenue that are tied to the economy, such as sales tax or income tax. Regression analysis is the most common approach to econometric forecasting.

Econometric forecasting is the only methodology that lends itself to projecting revenues or expenditures based on changes in the economy. Econometric forecasting using statistical theory can be more accurate than the other techniques because, unlike the best judgment method, it is based on behavioral relationships that can be measured and evaluated; it is not limited to forecasting in one direction like trend line techniques; and it considers multiple variables in making projections rather than the single variables used in deterministic techniques.

Forecasting is a complex task that requires a variety of skills and techniques. The accuracy of the forecast depends on the quality of the data, the choice of the method, and the skills of personnel doing the forecasting.

## FORECASTING PROCESS

This section will suggest methods for preparing medium-term revenue forecasts.

### Organization

Forecasting is a complex task that requires a variety of skills and techniques. The accuracy of the forecast depends on the quality of the data, the choice of the method, and the skills of personnel doing the forecasting.

- What is the intended purpose of the report?
- How many years are to be projected?
- When is the report due?
- Why do it? What benefits are expected?
- What resources are committed for the project and are they adequate? Staff, computers, other?

- Who is responsible for the project? Finance, budget, treasurer or city management?

Will the forecasts be prepared centrally or by department for the same revenue sources? or a combination of both? Centralizing the preparation offers advantages: consistent assumptions, fewer highly skilled people involved, and a uniform methodology applied to similar subjects. The disadvantages are: the central office may not have the data, knowledge, or experience to make accurate forecasts.

- Will the forecast project aggregate revenues or individual ones? Although it is possible to forecast in the aggregate, separate forecasts of each revenue source provide better control of the variables and allow more opportunities for analysis.
- Will the forecast project expenditures by accounting classification, departmental organization by program, or use a combination?
- What major assumptions are included in the forecast that must be applied uniformly? How will that be done?
- What data and information sources will support the project? Are they current, accurate, and available?

## Forecasting Revenues

Forecasting revenues is a complex task that requires a systematic approach. The following steps are recommended for developing a revenue forecast:

- Gather historical data—actual revenue collected for each source for at least the last five years and a description of the revenue source and its legal authority (one page for each revenue source).
- Ensure that the sum of the individual revenues still equals the actual grand total revenues at year-end.
- Clean data to eliminate rate changes, base changes, or other one-time events (i.e. large refunds). Retain the documentation of adjustments made to clean the data and why they were necessary.
- Analyze data and characteristics of the revenue source to determine the most appropriate forecasting methodology. Select the appropriate forecasting method and apply it to the data series to project the revenue for the applicable years.
- Determine if the revenue projection appears reasonable in the current context, then adjust it for known changes in the revenue source or the economy that may impact the revenue.

Major data sources for revenue forecasting include historical data, current data, and external data. The result of the forecasting process is a revenue forecast, which is a projection of future revenue.

## Forecasting Expenditures

Determining how classification is organized is the first step. The program forecast organization is important because it is the basis for gathering information from the central budget office or departments. Using the accounting classification system alone organizes the expenditure forecasts by personnel services, materials, services, transfers, and equipment. Shown at a city-wide level, this forecast is relatively easy to accomplish. With only five or six categories of expenditures to forecast, a deterministic or trend line approach is appropriate and can be done by the central budget office. While relatively simple, this framework provides no basis to analyze why expenditures are increasing or decreasing other than to reflect past years' trends or the assumptions made in a deterministic model. Dividing these major classifications into other expenditure sub-classifications provides more detail, more elements to forecast, and a potentially more accurate forecast. However, organization by accounting classification provides little explanation for the increase or decrease of an expenditure or which city program contributed to it.

Another way of organizing expenditure forecasting is to use an organizational approach based on the hierarchy of departments and divisions combined with existing accounting classifications. This orientation provides more detail to the forecast because expenditures are projected by department, division, and accounting classification rather than city-wide. A deterministic or trend line method is also appropriate in this approach. Forecasts built organizationally provide detailed information for analysis that is not available in a simple accounting classification approach. A key disadvantage of the departmental hierarchy organization is that it does not reflect information on a program basis.

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A second alternative is to prepare an exception-based forecasting system in which the forecaster establishes a constant level of service budget as a base line. Department or program managers advise the forecaster of changes or exceptions to this base line for future years based upon criteria given by the budget office. The detailed orientation of exception-based forecasting permits analysis of both the base and changes in subsequent years, makes better use of

department staff time, gathers critical information from knowledgeable sources about future year changes, and involves department personnel in the forecasting process. The disadvantage continues to be considerable staff time needed to put together forecasts of expenditures. Because this is a more effective method of forecasting expenditures, more time is devoted to this alternative.

The forecaster develops a base line constant level of service budget. Using the current year budget as a starting point, the forecaster adjusts the current budget so that it represents a true base line. Items subtracted are one-time purchases of capital equipment, supplies, and contracted services. Other items removed include one time personnel expenses of retiring or terminating employees ( i.e. payment for unused vacation, sick leave, or severance pay). Items added to the base are annualization of salary for employees who were funded in the base year for part of the year and merit pay for a portion of employees. With these adjustments, the forecaster sets the base budget for each department/program and sends it to departments for their review and projected future year program adjustments.

Forecasting expenditures is a continuous process. It is not a one-time activity. It is a process that is ongoing and evolves over time. It is a process that is ongoing and evolves over time.

- Mandated service level changes or costs due to local ordinances or policy changes
- Productivity increases approved by Council or city management
- Funding for costs of operating new capital facilities scheduled to be opened
- Funding for costs of services due to extensions of service area
- Funding for new and replacement equipment.

Forecasting expenditures is a continuous process. It is not a one-time activity. It is a process that is ongoing and evolves over time. It is a process that is ongoing and evolves over time. additions/changes are ultimately included in the expenditure forecast to best represent future years' current service committed costs. All approved changes are added to the respective base line budget by respective year and totaled. The resulting fiscal year totals represent projected expenditures. Items requested but not included in this forecast are shown on a separate list of unfunded needs.

[illegible]

The City of Dallas's 1995 Long-Range Financial Forecast is included as Exhibit 6-1.

This exercise has three parts. Using your data on the largest revenues for the current year, which forecasting method would you use for each of the largest ten revenues and why? Use the following format:

Proposed Forecast Method

## Rationale

## Forecasting Revenues and Expenditures 6-Ixix

Expenditure  
Rationale

Proposed Forecast Method

3. You have completed your first multi-year forecast, and it shows that your city is facing a 25% revenue shortfall in the first year, a 35% revenue shortfall in the second year, and a 50% shortfall in the third year. What steps would you take to prepare management and the Council for this fiscal problem?

**Exhibit 6-1**  
**City of Dallas**  
**Long-Range Financial Forecast**

## CHAPTER 8

# MISSIONS, GOALS, OBJECTIVES, AND MEASURES

### PURPOSE

The purpose of this chapter is to enable you to:

- Define the meaning of and understand the differences among missions, goals, objectives, and measures and their use in budgeting
- Write and evaluate mission statements, goals, objectives, and performance measures
- Prepare mission statements, goals, objectives, and performance measures for your jurisdiction.

### HOW THIS CHAPTER WILL BENEFIT YOU

Local government budgets increasingly reflect a rational basis upon which budget decisions are made. To make rational decisions, elected officials are seeking more information about the local government and the type and quality of services it provides. Including mission statements, goals, objectives, and performance measures in a budget, combined with financial information, is an effective way to meet the information needs of elected officials and the public while at the same time promoting rational decision-making. This chapter will introduce mission statements, goals, objectives, and performance measures and define them as they are used in budgeting. An example will be provided with an exercise at the end of the chapter to practice this aspect of budgeting.

### DEFINITIONS

The use of goals and objectives is usually associated with a “management by objectives” approach to budgeting, or

*program budgeting*. Program budgeting is a technique that relates revenues and expenditures to public goals by asking:

- What is to be achieved?

- What programs are to be initiated or terminated, expanded or reduced?

The goal can provide the answers, goals, objectives, and the following describes the concepts in **Mission Statement**

**Regional Water Utility District of Dallas (DWU)** is a City-owned enterprise providing regional water and wastewater services, and works in support of the goals of the City of Dallas, while striving to provide excellent responsiveness to the needs of our customers at a fair and reasonable cost through our operations, customer service, maintenance, and support functions.

## Goal

A goal is the long-range desired outcome of specific activities. The combined goals are a definitive statement of the purpose of an organization. A goal has the following characteristics: it is general, timeless, continual, and often never fully achieved. The goal of an organization is the unifying point around which all activities revolve. In a public organization, goals are associated with each of the major services offered. Goals provide a framework within which the organization operates.

For example, the program goals of DWU's Water Operations are:

- To ensure adequate water pressure for fire protection.

## Objective

Objectives are the primary decisions that will be made to achieve the goals. They are identifiable, measurable, and quantifiable, so that the impartiality and objectivity of the decision-making process are enhanced. Quantitative measurement of objectives is very important, and every effort should be made to meet this requirement. Examples of objectives for water operations include:

- To provide aesthetically pleasing, quality water that meets customer demands for water quality and regulatory standards
- To perform water distribution system maintenance efficiently and effectively, minimizing the impact on customers' water delivery
- To maintain water system pressure at or above legal requirements
- To provide timely and accurate analysis to ensure all regulatory requirements are met.

## Measures

Measures are the primary decisions that will be made to achieve the objectives. They are identifiable, measurable, and quantifiable, so that the impartiality and objectivity of the decision-making process are enhanced. Examples of measures for water operations include:

*activity-based measure* is a means of measuring an identifiable action or operation conducted or performed by an organization. Activities are performed to achieve identifiable objectives of a program. There are two types of activity-based measures used in budgeting.

• **Demand measures** quantitatively indicate *work to be done* by assessing the severity of a problem or scope of the work to be performed. Sometimes the demand measure is helpful in showing the size of a problem to be addressed, while the following measure can be used to show how much will be accomplished in the first year of a multi-year program.

• **Workload measures** quantitatively indicate how much *work is accomplished*, which represents the simple counting of the units of work completed. This indicates the size of a

program by measuring the number of units involved. Workload measures can serve as the output side of an efficiency measure. (See below.)

*A performance-based measure* is a way to measure by *efficiency or effectiveness* the achievement of an identifiable action, operation, or program performed by an organization.

•**Efficiency measures** indicate the accomplishment of desired results with little wasted resources (i.e. minimum cost). They measure how economically resources are being utilized using a *ratio of input* (costs or resources) to the *ultimate output* (service or units of production). Efficiency measures are usually expressed as cost per work unit produced, cost per customer, cost per employee hour, units produced per hour, or as some other expressed relationship between production and resources. Measures of efficiency do not usually provide an indication of the quality of the product.

~~Efficiency measures of Water Operations~~ Efficiency measures of Water Operations are in terms of accepted standards within an activity, for

- Cost per million gallons treated
- Cost per mile of main maintained
- Cost per million gallons pumped
- Cost per sample analyzed.

Efficiency measures for other government services might include:

- Cost per 1,000 residents (instead of cost per resident)
- Cost per metric tons collected
- Cost per million liters processed
- Cost per revenue passenger
- Operating cost per substation
- Cost per inspection
- Cost per kilometer of streets swept or cleaned
- Cost per kilometer of sewer cleaned

Efficiency measures are

*process oriented*, not results oriented. Efficiency measures are useful in comparing one jurisdiction's per unit costs to those of other cities or private contractors.

•**Effectiveness measures** indicate the value or *quality of the product or service* provided. Effectiveness measures provide an indication of how successfully government programs are applied to perceived problems, needs, or objectives. Effectiveness measures tend to be more

subjective than efficiency measures because value judgments are involved. However, effectiveness measures should be quantifiable whenever possible. Effectiveness measures focus not on the process, but on results.

~~Water Operations~~ ~~Examples of effectiveness~~ effectiveness measures (with a quality objective shown in parenthesis) for

- Percentage of Water Samples meeting federal standards (health hazards)
- Percentage of citizens who rate the City supplied water as satisfactory on appearance, odor, and taste (aesthetic quality)
- Percentage of persons who made a complaint or requested service who were satisfied with the response by type of request or complaint (service adequacy and responsiveness)
- Percentage of fire hydrants surveyed that meet static water pressure requirements (flow adequacy)
- Percentage of samples analyzed accurately within a specific number of days (service adequacy and responsiveness).

~~Some Waste~~ effectiveness measures for local government might include:

- Percentage of citizens satisfied with service (pleasing aesthetics)
- Rate of injuries to waste collectors (employee safety).

Transportation

- Percentage of citizens who rate public transport as satisfactory or above when asked about their ability to arrive at their destination within a reasonable amount of time (accessibility)
- Gross number of deaths and injuries caused by traffic accidents and the rate per 1,000 population (safety)
- Percentage of streets with road surface conditions rated as satisfactory (comfort)
- Percentage of residents not within a specific distance from public transit service (accessibility of service).

## CRITERIA FOR EVALUATING MEASURES

~~PROCESSES ARE NOT THE SAME AS RESULTS. THE PROCESS OF EVALUATING MEASURES IS AN ONGOING PROCESS. MEASURES SHOULD BE CONSIDERED.~~

### Efficiency Measures

- Does the measure provide a ratio of inputs (cost or full-time equivalent workers) to a unit of outputs (workload)?
- Does the measure focus on process rather than results?
- Is the measure expressed in accepted standards within a program? For example:  
Cost per 1000 residents  
Cost per 1,000,000 hits processed

### Effectiveness Measures

- Is the measure results oriented, rather than process oriented?
- Does it measure progress toward a stated government goal or objective? (purpose)
- Does the measure relate to an objective of that service? (appropriateness)
- Does it measure the degree in which the customers need is met? (validity)
- Does it measure a characteristic that no other measure encompasses? (uniqueness)

- Does the measure cover all the objectives listed? (completeness)
- Is the measure simple and easy to understand? (comprehensibility)
- Are cost and staffing requirements for collection reasonable? (costs)
- Does the measure reveal problems soon enough that they can be fixed? (timeliness of feedback)
- Can accurate and reliable data be obtained? (accuracy)

## EXAMPLES

Effectiveness measures are those which attempt to measure the degree to which a program or service is achieving its intended purpose. The following examples are for informational purposes only and are not intended to be used as a model for developing measures. They are provided as examples of how measures can be developed and used in the context of considering the use of effectiveness measures to improve local government decision-making and communication with citizens.

## PRACTICAL EXERCISE

Display your jurisdiction's goals for the department with which you are working and complete the following:

---

Harry P. Hatry, et al. *How Effective Are Your Community Services, Procedures for Measuring Their Quality*, second edition. Washington, D.C.: Urban Institute and ICMA, 1992.

2.

**Programs** and three objectives for each program.

Effectiveness of the program and its effectiveness in achieving the objective and prepare one efficiency and one

b.

2.a.

b.

3.a.

b.

Effectiveness of the program and its effectiveness in achieving the objective and prepare one efficiency and one

**Exhibit 8-1**

**Example of Effectiveness Measures —Solid Waste Collection**

**Source: *How Effective Are Your Community Services***

## CHAPTER 9

# PREPARING FOR PROGRAM BUDGETING

## PURPOSE

The purpose of this chapter is to enable you to:

- Identify the budget format types commonly used by local governments
- Describe the characteristics unique to program budgeting
- Understand the steps needed to prepare a program budget
- Determine the total cost of a program
- Identify other organizational impacts inherent in program budgeting.

## HOW THIS CHAPTER WILL BENEFIT YOU

State laws and city charters in the United States establish general requirements for local government budgets. These requirements vary from jurisdiction to jurisdiction. For example, the city charter in Dallas, Texas, specifies the position responsible for preparing the budget; the date the budget should be submitted to Council; the start and end dates of the fiscal year; and the budget powers of the City Council to include approving the budget, setting tax rates, approving fees, incurring debt, and amending the budget, if necessary. Cities, with their home rule\*\*\* (Define)\*\*\* powers, are fairly independent entities with considerable authority and latitude to control their own destiny. Budget format type, content, organization, and overall style are determined by local government officials. This explains why no two U.S. local government budgets are the same. Local government budgets reflect the needs and requirements of the communities they serve.

This chapter explains how to prepare a program budget for a local government. It also explains how to prepare a program budget for a local government.

management accountability, operational effectiveness, or financial planning. This chapter explores that possibility and provides guidance in developing a program budget format.

## TYPES OF BUDGET FORMATS

Single- and multiple-purpose budget formats present budget information from different perspectives. The format type is an important decision. Different perspectives on the information will prompt different questions from policy-makers about the budget. Producing a budget with information presented in different formats improves decision-making and management and helps the budget to serve multiple purposes.

### Line-Item Budgeting

Line-item budgeting is the most common type of budget format. It presents budget information in terms of expenses or costs. The primary classification of operating expenses usually includes: personnel services, supplies and materials, services and other charges, equipment or capital outlay, and reimbursements. These can be broken down into more detailed expenditure accounts or object codes. For example, personnel services include salaries, pension, benefits, and temporary help. Supplies and materials include office supplies, utilities, fuel, or minor machinery. Revenues are also divided into primary categories by source of revenue such as taxes, licenses and permits, interest earnings, intergovernmental revenues, fines and forfeitures, charges for services, inter-fund revenue, and miscellaneous revenues. The accounting system provides a numerical coding system for each expense item and revenue source. Revenue and expense codes may number in the hundreds depending upon the size and complexity of the jurisdiction and the level of detail required in the budget and accounting to meet legal and management requirements.

Line-item budgeting is control-oriented. Its detailed construction allows control of almost every level of spending. Discretion to spend is limited to the authorizations set aside in the accounts to ensure that funds are disbursed only for the purposes stated in the adopted budget. This type of budget is easy to prepare and shows how much money is set aside for each specific item of cost. However it does not provide information about the activities or functions of a local government's departments, programs, or activities.

## Activity Budgeting

Activity budgeting is a control-oriented budgeting system that provides information about the activities of a local government. For example, an activity budget for a police department might break the department into activities such as patrol, criminal investigations, special operations, staff support, and administration. Activity budgets do occasionally include specific goals and objectives for each unit.

Activity budgeting is a control-oriented budgeting system that provides information about the activities of a local government. For example, an activity budget for a police department might break the department into activities such as patrol, criminal investigations, special operations, staff support, and administration. Activity budgets do occasionally include specific goals and objectives for each unit.

## Program Budgeting

general government. The programs that make up leisure services might include libraries, recreation services, parks operation and maintenance, cultural and arts facilities support, zoos, and recreation programs for senior citizens.

Program budgeting emphasizes the planning aspect of budgeting and seeking choices between services based on the

*output* of the service. Public goal setting is a part of the planning and prioritizing process. Allocating resources to achieve those priorities improves the decision-making process and represents a more rational basis of allocating resources.

Program budgeting is useful in grouping like activities together, eliminating duplication of programs and highlighting potential gaps in a city's approach to a problem. However, it is more complex than line-item budgeting. Complicating factors include: (1) determining the total cost of programs, (2) defining programs that are difficult to conceptualize and difficult to monitor, and (3) the need for computer based accounting and information systems to handle accounting for both legal basis budgets and program budgets. Additionally, program budgeting requires staff with analytical skills both in departments and at the central budget office to prepare and justify the supporting program budget documentation and critically review program budgets when submitted. These factors need to be considered prior to adopting a program budgeting system. It is also suggested that program budget implementation should be undertaken in small steps over three to four years consistent with available resources.

In Poland, the central government has established a uniform set of accounts and codes relating to National Budget Law chapters, sections, and paragraphs. The budget titles resemble programs and include Construction works, agriculture, transport, communication, public utilities, housing and communal services, education, culture and arts, health care, social assistance, sport, civil defense, state and local administration, security, finances, and economic development grants. This predisposition to organizing around programs may reduce the impact of changing from a traditional budget to a program based budget format.

## Performance Budgeting

Performance budgeting is a budgeting system that focuses on the results of programs and services. It is a type of program budgeting that uses performance measures to allocate funds. Performance budgeting has some of the characteristics of program budgeting. Like program budgeting, performance budgeting uses a program structure and allocates funds to programs within an organization based on overall goals and program priorities. However, performance budgeting is unique because it identifies the service level upon which the budget is based. Service level is described as the use of performance measures and statistics. Performance measures for a Street Operations program might include the following:

Input measure:	Money
Output measure:	Street lane miles completed
Efficiency measure:	Cost per street lane mile
Outcome measure:	Percentage of streets in satisfactory condition

The performance budget aims to improve the management of programs as well as to control costs. The emphasis upon performance measurement and statistics is an effective tool for improving management operations. However, this method requires extensive data gathering throughout the organization, and the associated cost of that should be considered in implementing such a program. Performance oriented budget should be implemented in small steps and spread over three to four years consistent with available resources.

U.S. municipalities are generally free to choose a budget format type. But the choice is not one pure form over another; rather, budget officials are more apt to combine budget format types to suit the Council, management, and jurisdiction's needs. As a result, there is a more practical approach to selecting a budget format—use what meets your needs and works in the jurisdiction. As a noted budget scholar once said, "These formats do not exist in reality; they exist only in ideal forms and, as such, will continue to exert influence over the minds of budget makers."

## STEPS FOR PREPARING A PROGRAM BUDGET

~~The budget process starts with planning or budget, like program budgeting, plans first programs and~~  
**Determine Overall Goals and Spending Objectives**

The Council plays a major role in the program budget process at this step by providing formal guidance to management on goals and program priorities. Goals represent strategic direction as to what is important. For example, the Council sets the tone or direction for the budget by indicating that the budget may not increase more than a specified percentage over the current year or that taxes will not be increased in the next year. Alternatively, the Council might establish a list of programs where improvements and additional funding or funding reductions are needed.

~~General guidance and the individual goals, establish the departmental fiscal targets, and refine~~  
**Translate Objectives into Operational Programs**

~~With this guidance, the Council can then establish the departmental fiscal targets, and refine~~

## Plan the Budget

Preparing the budget is the first step in the process of planning and controlling the organization's financial resources. The budget is a plan that responds to Council direction and allocates resources to bring about change in the future. By identifying program priorities and allocating funds to them, a series of annual funding decisions can produce results in a subsequent year.

## Calculate Financial Requirements

Developing a budget is a complex task that requires a high degree of coordination and communication. The budget is a plan that responds to Council direction and allocates resources to bring about change in the future. By identifying program priorities and allocating funds to them, a series of annual funding decisions can produce results in a subsequent year.

## Measure Effectiveness

Measuring the effectiveness of a program is a complex task that requires a high degree of coordination and communication. The budget is a plan that responds to Council direction and allocates resources to bring about change in the future. By identifying program priorities and allocating funds to them, a series of annual funding decisions can produce results in a subsequent year.

## Audit Programs

The following audit programs are provided for informational purposes only. They are not intended to be used as a substitute for the audit program of the auditor.

## DETERMINING TOTAL COST OF A PROGRAM

The total cost of a program is the sum of the direct and indirect costs of the program. Direct costs are those costs that are directly attributable to the program, such as salaries, benefits, and other personnel costs; travel; contracted services, commodities, and supplies of a consumable nature; fixed obligations; and fixed charges. Capital outlay includes equipment, fixtures, and other tangible property that has an expected useful life of more than one year and whose cost exceeds some predetermined value.

Indirect costs are expenses of the program related to other agencies' or departments' cost of providing services to a program. These indirect costs represent, for example, the program's pro-rata share of departmental administrative expenses or city-wide central support expenses from finance, legal, and other support departments. The budget office determines to what extent indirect costs are distributed for budget purposes.

To estimate the total cost of a program for budget purposes, the following steps are suggested:

- Determine the number of units of service or work to be accomplished in the fiscal year.

- Determine the number, classification, and salary or wage scale of the personnel needed to accomplish the program for the fiscal year to meet the stated objective and calculate the program personnel costs. Determine whether any of the personnel are less than full time employees or will work less than a full year. An easy way to calculate these totals is to develop a salary worksheet using a computer spreadsheet program that will permit all the variables to be considered for each person and produce an estimated salary cost for the program.
- Using rates from the budget office, determine employee fringe benefit costs, pensions, and need for temporary help.
- Use budget office estimated rates, usage, and allocation schedules to determine the program's cost for utility services (gas, electricity, and water consumption) and other fixed costs.
- Estimate the costs of other operating expenses such as supplies, commodities, and services (i.e. cleaning, vehicle use and maintenance, or office supplies).

**Note:** Budget offices may specify the method used to calculate the above operating expenses. For example: a *unit cost* method compares the volume of work anticipated to the items needed to complete the work, and funds are budgeted to purchase these items. A *pre-determined charge* may be specified to cover costs for property and liability insurance, maintenance of equipment, janitorial services, computer services, or central supply stocks. A *standard cost* table may be developed to forecast expenses of predetermined items such as standard costs of supplies for a new position, furniture complement needed for a new position, costs of maintaining a building, cost of operating a government vehicle per kilometer, etc.

- Determine the need for new or replacement equipment. Expenses related to purchase of equipment are naturally a part of the total cost of the program; however, large one-time purchases may distort the program cost from year to year. Budget offices usually provide direction on how to handle this issue so that it is done uniformly across the city.
- Calculate indirect costs. Generally, the department or the budget office makes these determinations and advises program managers of the basis for calculating them. Distributing the cost of department overhead among programs simply means calculating the cost of department administration, secretarial, clerical, and administrative support and spreading the cost among the several programs based on a formula. A formula is determined after analyzing the nature of overhead services provided to each program and determining the most appropriate basis for allocation. These costs might be allocated on the basis of personnel staffing, personnel cost, work load or other means. Budget offices may specify how these costs will be allocated for all departments for uniformity purposes.

- Provided that the proposed officers of the club shall not be persons who are disqualified from holding office under the provisions of the Societies Registration Act, 1860, and the Societies Registration (Amendment) Act, 1926.

Program budgeting impacts other aspects of the organization. It depends upon a decentralized budget development and management process and requires the traditional roles of the budget office staff and budget analysts to change. Addressing these issues early in the preparation process is critical to implementation success.

office—it resides with the program manager in a department. To make program budgeting work, the responsibility for budget development should rest with a department manager.

From this, the following can be deduced: the influence of the number of people singing on the pitching

the training, the size of the organization and the amount of detail requested in the budget instructions are important considerations in designing a training program and determining who should be trained. Also, you should remember that many of these personnel have never prepared a budget before now. Training programs should be geared to the participants involved in the budget and may require separating directors from program managers and analysts. Training should be placed early in the schedule to allow time to train all the people involved and still leave enough time to perform their new responsibilities.

On the other hand, different skills and responsibilities in budgeting preparation should be assigned to plan and coordinate the budget preparation and execution process. In smaller departments, this may be an additional responsibility added to one person's other administrative duties. In larger departments, the scope of responsibilities may require that a full-time budget analyst be assigned this duty. Similarly, the added responsibilities placed upon program managers for budgeting and managing for results may be beyond the capabilities of the incumbent, who may not have the management skills to effectively carry out these new responsibilities. Management needs to consider these two issues as program budgeting concepts are implemented.

Generally, the benefits of decentralized program budgeting exceed the costs, and the organization that implements decentralized program budgeting increases its efficiency, effectiveness, and accountability.

## **New Roles**

Typical tasks of the budget office include developing the program justification, reviewing the program justification, providing training for the department management and budget personnel, ensuring that instructions are followed, conducting budget reviews, and finally, consolidating and publishing the final budget.

Many new roles will be created for the budget office as program budgeting is implemented. The budget office will be responsible for developing the program justification, reviewing the program justification, providing training for the department management and budget personnel, ensuring that instructions are followed, conducting budget reviews, and finally, consolidating and publishing the final budget.

prove program analysis and descriptions. After the budget is adopted, the budget analyst not only monitors budget execution but works closely with program managers as they report on program implementation for management.

What are the objectives of the program budgeting model? The objectives of the program budgeting model are to provide a systematic and logical process for developing and managing the budget, to ensure that the budget is based on the program's needs and objectives, and to provide a framework for monitoring and evaluating the program's performance.

## KRAKOW'S PROGRAM BUDGETING MODEL

The following are the essential elements of the Krakow program budgeting model:

- Dividing local government into basic units called budget tasks
- Calculating budget tasks (direct and indirect)
- Completing an action plan for each task (including workload and performance measures)
- Allocating resources based on highest need and utilization
- Questions asked to develop the model:

What are the priorities?

What are the objectives for next year?

## EXERCISE

At the end of the manual is a case study developed by the City of Krakow on task budgeting. Related exercises are included with the Krakow case study in the final section of this manual.

## CHAPTER 10

# REVIEWING AND ANALYZING BUDGET REQUESTS

## PURPOSE

The purpose of this chapter is to enable you to:

- Understand the changing roles and responsibilities of the Treasurer and budget staff in budget reviews
- Understand differences between U.S. and Polish budget reviews
- Identify three perspectives in which a budget request will be reviewed
- Identify issues that need to be considered in reviewing department budget requests.

## HOW THIS CHAPTER WILL BENEFIT YOU

Departments in the United States are not responsible for revenue generation, which is rarely the case. Because most departments are not responsible for revenue generation, they tend not to be constrained in their budget requests. Nor do citizens feel constrained by revenue constraints when making budget requests. This means that needs always significantly exceed the resources available, and a review process is needed to determine which needs will be funded and which will not.

Finally, the State of Ohio has a long history of budget review, and the process of reviewing budget requests is a well-established one. This chapter will provide you with the information you need to understand the process and to participate in it effectively.

## ROLES AND RESPONSIBILITIES

Preparing a local government budget is a significant undertaking involving many participants: elected officials, appointed executives, department directors and managers, and budget staff. Size and complexity of the organization are factors in deciding whether the annual budget is prepared centrally by the Treasurer and budget staff or decentralized with city departments and enterprises formally submitting budget requests to the Treasurer and budget staff for consideration. With the continued shift of additional responsibilities to gminas and elected and appointed officials' interest in improving operations and efficiency through the budget process, city departments and enterprises will continue to play a important role in the budget process. This chapter focuses on a decentralized budget development and review process.

~~The City Board and City Board staff have the following responsibilities in the budget review process:~~

- analyzing detailed department and program budget requests and performance information,
- managing an expanded budget review process, and
- maintaining close coordination between City Board, budget staff, and department directors.

~~The City Board and City Board staff have the following responsibilities in the budget review process:~~

- analyzing department budget requests based on Council priorities and the effectiveness of department operations,
- providing the Treasurer and City Board with detailed and specific information about department activities,
- serving as a liaison to specific departments for budget matters,
- serving as experts on city finances and statutory budgetary requirements, and
- serving as budget and management analysts for the Treasurer or budget officer.

In developing a decentralized process, the close involvement of departments in the budget process is essential. For the budget staff, the department and enterprise directors are the best source of information about the city's financial history and the persons best suited to identify service needs. From the department perspective, the budget process is a useful way to advise the Mayor, City Board, and Council about their programs, alternative approaches to providing services, and special problems facing the department.

## REVIEWING BUDGET REQUESTS

Budget staff conduct the first review of department requests. The department directors conduct the second review, the Chief Executive (Mayor/City Manager) conducts the third, and the legislative body—the Council—conducts the last. Knowing that the request undergoes such scrutiny, department directors need to be prepared to defend the requests at subsequent review sessions. Experience has shown that only fully justified budgets and adequate preparation can survive the process. Budget reviews tend to be formal presentations followed by questions from the reviewers. A written record of budget decisions is made at each step in the review process and used to track the status of the budget request from beginning to end.

gmina leaders to compare task efficiency and effectiveness. Much of the background information is presented orally, and there is no recorded basis for decision-making.

~~\_\_\_\_\_~~  
operating costs. Included in minimum operating costs are mandatory expenditures (obligatory and delegated assignments from the central government) and base or current service expenditures of a department's continuing operations (gmina responsibilities by law) plus an inflation adjustment. Other discretionary costs or budget requests (enhancements in operations) are identified in a budget supplement. Preparing department budget requests based on written instructions and requiring that they be based on minimum operating costs enhances the ability of the city to review budget requests and helps management make better decisions. Separating enhancements from the base service level permits these items to be more thoroughly analyzed and added to the budget based upon individual merit.

~~\_\_\_\_\_~~  
Expenditure of the program is displayed by the new program, identifying the budget requirements for the budget.

- detailed explanation of the program inputs and outputs
- planned program emphasis and changes in emphasis
- crosswalks (computerized links between budgeting formats)
- program and financial plans.

To get the maximum benefit from a budget review, the department director should be permitted to present the departmental budget request in a formal budget review. The focus of this review is to gain an understanding of existing and planned management policy changes as reflected in the budget request. Budget reviewers use this opportunity to obtain additional clarifying information about a budget request, and the department should provide oral or written answers to the request.

This means that the department director should be permitted to present the departmental budget request in a formal budget review. The focus of this review is to gain an understanding of existing and planned management policy changes as reflected in the budget request. Budget reviewers use this opportunity to obtain additional clarifying information about a budget request, and the department should provide oral or written answers to the request.

## PERSPECTIVES ON BUDGET REVIEWS

This means that the department director should be permitted to present the departmental budget request in a formal budget review. The focus of this review is to gain an understanding of existing and planned management policy changes as reflected in the budget request. Budget reviewers use this opportunity to obtain additional clarifying information about a budget request, and the department should provide oral or written answers to the request.

- discretionary rather than mandatory
- large rather than small
- increasing, rather than decreasing or stable.

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## Treasurer/Budget Staff Review

As the complexity of the budget increases, so does the importance of the Treasurer and budget staff in reviewing and preparing the budget. The budget staff not only have to keep the needs of the departments in mind when reviewing budgets, but must also consider the City Board and the Council guidance.

When a budget request is submitted, the reviewers assist the Treasurer by analyzing the request based on Council, Treasurer, and budget office guidelines and instructions. The reviewers take their direction from management and may perform different roles in reviewing budget requests.

- In a

*compliance* role, the reviewer verifies that the request conforms to budget guidelines and preparation instructions of the budget office and that all requested information is included and appropriately completed. For example, the reviewer ensures that proposed expenditures are coded to the correct standard accounting classification code and that the request is mathematically correct.

- In an *analytic* role, the reviewer focuses upon budget requests that provide detailed program information beyond that required by the State obligatory budget format. This may be the task budget approach used in Krakow or additional program detail as used in Lublin or Szczecin. Detailed budget information including program descriptions, expenditures, and performance measures is assessed and analyzed. The purpose of the review is to fully understand the program, its objective, and the likelihood for its success. The analyst is encouraged to ask management questions and analyze these requests for compatibility with overall priorities and objectives established by Council.

- In an *advisory* role, the reviewer checks the proposed expenditure requirements to determine their adequacy and need for changes, if any. It is understandable that mandatory expenditures are uncontrollable and must be funded in the budget. The reviewer normally analyzes these

requests to ensure that the department programs have sufficient allocations. For base or current service expenditures, the reviewer analyzes requests to ensure that there are no increases in these items without sufficient justification. The reviewer checks discretionary items more closely than either mandatory or base expenditures. These are the items that are funded only if resources are available.

### **When the City Board Reviews the Budget**

the City Board's review should also focus upon other aspects of the budget. Specifically:

- That the budget recommendations are appropriate and take into account all the financial and management policies/directives addressed earlier in the budget development process by the Council and later in budget reviews. This serves as a check to make sure all policies are being adhered to.
- That the budget does not contain any excessively controversial issues recommended to the Council.

## City Council Review

The Board's review is subject to two important caveats: (1) the quality of the

The Board will have a budget in 2016 that is essential to the City. By Board approval, the Board is to approve the budget in the budget preparation and review process, then the Council should be comfortable with the budget as presented.

University of Tennessee, College of Business Administration, Knoxville, TN

These projects are also being funded by the City of Knoxville through the budget process. These projects were included in the budget. This means not only city-wide budget priorities but may also include specific Councilors' priority projects for certain constituents or geographical areas.

**Finally, the Council wants to be convinced of the budget pibbess. If there is a danger that the budget tails**

## BUDGET REVIEW CONSIDERATIONS

The Treasurer and budget staff are charged with the responsibility to review and analyze department budget requests and to recommend and draft a budget plan for the City Board's review. Budget staff, who are responsible for reviewing departmental budget requests, need to perform more than compliance checks against budget guidelines and instructions. The budget staff should act as budget and management analysts, asking management questions and analyzing budget requests. Following are some questions that the budget staff and budget officer should keep in mind as department budgets are reviewed.

## **General**

- Do the proposed performance and service levels justify the budget request?
- Are the spending requests credible? Are they based on valid assumptions?
- Is the proposed approach to a particular service the best way to achieve the stated objective?
- If choices must be made between competing budget requests, what is the relative importance or value to the community of the new spending programs proposed by the various departments?
- By spending more on a particular service during the next fiscal year, will the gmina save money in the long run?
- Is there duplication of work between departments? Can services be improved or costs reduced by changing staffing patterns or other revisions?
- Is the proposed level of financing adequate for each service?
- Will the estimated revenues that will be available to the city during the next fiscal year be sufficient to fund basic services at an acceptable level? Should the Council consider increasing revenues?

## **Programs**

- Have programs been defined?
- Have the objectives of new and expanded programs been clearly defined?
- Have all significant increases or decreases been explained?
- Have efforts been made to reduce costs through improved work methods, automation, or better personnel utilization?
- Have priorities been assigned to new and expanded programs and to equipment?
- Have fees and charges for rendering services been compared to the cost of providing the service or enforcing the regulations?

- Have major problems encountered during the year been explained?
- Have economies achieved during the past year by improving work methods been explained?
- Are there any recommendations for further reducing costs and increasing the efficiency of the operation?
- Are there any recommendations regarding changes in the level of services?
- What were the effects of budgetary limitations last year, if any?

### **Personnel**

- To what extent do the requested positions relate to defined activities and programs? Does an evaluation of duties and responsibilities support the need for new positions?
- Have provisions been made for delay in filling new and vacant positions?
- Does the opening of new facilities justify the need for the personnel in the operating budget?
- Have employee turnover, overtime, seasonal personnel, leaves of absence, and the need for related appropriations been considered?

### **Services**

- Regarding contractual services, have expenditures and workload data of previous years been carefully examined?
- For each specific service to be rendered, is the need and the manner of pricing explained? Has the level of service been examined to evaluate present methods?
- Are contributions to non-governmental agencies based on requests supported by detailed information about the service being provided? Has the effectiveness of such services been evaluated?

### **Materials and Supplies**

- Is an analysis of the expenditures and consumption of previous years included with requests for material and supplies?

- Have price increases and supplies required by additional personnel been considered? Does the need for additional supplies relate to increased workload or new and expanded programs? Have inventories been reviewed?
- Are there inventory or other controls over the use of supplies? Have work methods been evaluated along with the type and quality of supplies?

## **Equipment**

- Has equipment been proposed that will increase or decrease operating costs next year and beyond? Which equipment investments have the highest priority?
- Has equipment been identified as replacement or new? Has the condition of the equipment being replaced, as well as its potential trade-in value, been reviewed? Have inventories of existing equipment been checked to determine the need for new equipment?
- Have work methods, as well as the experience of other gminas in using special types of equipment, been reviewed? Are requests for new equipment compatible with expanded work programs or possible savings?
- Have equipment needs of new personnel been considered?
- Have repair costs, along with the advantages of leasing, been analyzed?

## **Reserves**

- Has the amount of the reserve fund (i.e. the amount of uncommitted money expected to be left over at the end of the next fiscal year) been reviewed?
- Is the amount of the reserve fund adequate? Should additional funds be set aside for emergencies?

After considering these items for each budget request and the budget in general, the Treasurer and budget staff should be able to prepare a draft budget for the City Board bringing together estimated revenues and proposed expenditures for the next fiscal year into a comprehensive budget for the gmina.

## PRACTICAL EXERCISE

For the following program, examine the information and explain the questions that should be raised and why they should be raised. All costs have been adjusted to remove inflation impact.

1. In a senior citizen's folk dance program sponsored by the Department of Culture, the following cost and attendance information was gathered:

<u>Year</u>	<u>Cost</u>	<u>Attendees</u>
1990	20,000 z_	700
1991	21,250 z_	740
1992	23,750 z_	760
1993	25,000 z_	755
1994	30,000 z_	750
1995 budget	35,000 z_	745
1996 proposed		45,000 z_      —

2. In the same type of program, a similar gmina had the following costs and attendees for the same years:

<u>Year</u>	<u>Cost</u>	<u>Attendees</u>
1990	17,500 z_	200
1991	25,000 z_	1,200
1992	25,000 z_	1,080
1993	26,250 z_	1,200
1994	26,875 z_	1,300
1995 budget	26,875 z_	1,800
1996 proposed		30,000 z_      —

What tentative conclusions seem warranted? What follow-up questions seem appropriate?

## CHAPTER 11

# PREPARING THE BUDGET DOCUMENT

## PURPOSE

The purpose of this chapter is to enable you to:

- Identify differences between U.S. and Polish budget systems and documents
- Determine what elements should be included in the budget document
- Compare your budget document against criteria for distinguished budget presentations.

## HOW THIS CHAPTER WILL BENEFIT YOU

What budgeting differences exist between the U.S. and Poland? How do U.S. and Polish budgeting practices differ? This chapter provides a detailed comparison of U.S. and Polish budgeting practices and documents. Lastly, the chapter includes a series of questions to determine how your jurisdiction's budget meets criteria for evaluating budget documents. This assessment is helpful in identifying what aspects of your budget document could be improved and how those improvements could be accomplished.

## BUDGET DOCUMENTS—A COMPARISON

Budgeting in the U.S. and Poland differs significantly. In the U.S., the federal government and the states have separate budget documents. In Poland, the central government and the local governments have separate budget documents. This chapter provides a detailed comparison of U.S. and Polish budgeting practices and documents.

- Operating expenses and investment expenses are separated into two documents—an operating budget and capital budget.

- The operating budget is composed of various types of “funds” that relate directly to accounting standards required of local governments. A fund is defined as “an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and other resources together with all related liabilities, obligations, reserves, and equities that are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations.”

- The operating budget includes the following type of funds: General Fund, Debt Service, Enterprise and Fiduciary Funds. A brief definition follows:

**General Fund:** This is the main operating fund for the city. It accounts for basic services provided to the public and revenues that support the general operation of local government.

**Enterprise Fund:** These funds are fully supported by charges for services. Each fund establishes revenue-based fees and charges based on recouping the cost of services provided.

**Debt Service Fund:** Sometimes referred to as Interest and Sinking Funds, these funds account for the accumulation of financial resources to meet the principal and interest requirements of municipal bonds and debt service reserves that finance the city’s capital improvement programs.

**Fiduciary Fund:** This fund accounts for assets held by the city in a trustee or agency capacity. For example, grants from the national government or private donors would be accounted for in these funds.

- The budget document format is generally left to the discretion of local government officials, not prescribed by law.

- The budget serves as a policy document, financial plan, and operations guide and a communication device.

- The budget document includes program descriptions, multi-year comparisons, and performance measures to explain the budget, provide historical cost comparisons, and meet the information needs of different audiences.

- Budget documents that meet certain criteria are recognized with an award by an association of government finance officers.

During the last few years, changes in England and the structure of local government have transferred powers from the

the central government to local self-governments, reshaped the legal forms for city organizational units including budgetary units and enterprises, and encouraged decentralization of administration, financial and management systems.

Traditionally, gmina budget documents adhere to the central government's budget law regarding document format and content. Some of these requirements or characteristics include:

- Budgets are prepared in accordance with central government budget law.
- Operating expenses and investments are combined into one budget document.
- A single fund accounts for incomes and expenditures of the gmina—a General Fund. This includes grant funds received from central government and user fees and other revenues from local services.
- The budget document serves as only as a financial plan. Gminas prepare the document using a format and standard accounting classification codes required by the central government to meet their budgeting and accounting requirements. Few narrative descriptions and multiple year comparisons are provided to help explain and justify the budget. Comparisons of annual revenues and expenditures are generally limited to the current year and the proposed budget year.
- There are no external incentives or means of recognizing improved budgeting practices or documents.

Some gminas have begun to develop a task-based budgeting system. This approach is based on the concept of a task-based budget (in addition to complying with the obligatory state budget requirements). Developing the budget at a lower level (i.e. task) is designed to improve the allocation of scarce resources and help managers of departments improve the effectiveness and efficiency of city services. Exhibit 11-1 illustrates the budget information included in the Krakow budget for a specific task. The case study (in the final section of this manual) will illustrate the benefits of this approach in more detail.

- Including a message from the Mayor in the budget document. The budget message briefly describes the environment in which the budget was developed, the assumptions made in the budget, and recommendations included in the budget. It may also indicate the impact of those

recommendations. The message usually includes a summary of revenues and expenditure levels with explanations of year to year changes. Exhibit 11-2 shows the Budget Message included in Krakow's budget.

- Including budget charts and graphs in the document can be a important aid to the reader. It helps the reader understand important relationships, stimulates interest, and can focus the reader's attention on specific points of information. See Exhibit 11-3 for Lublin's use of pie charts in describing the sources and uses of funds.
- Preparing a highly condensed version of the operating budget document (sometimes called the Budget in Brief or Citizen's Guide to the Budget) is an effective way to communicate with citizens concerning the budget. It can also reduce the cost of producing a more costly budget document. This condensed version does not replace the Council approved budget document but only summarizes it. Exhibit 11-4 includes the Budget in Brief prepared by the City of Szczecin.

These are a few of the elements of the budget document that can make an effective budget presentation. Ideally, all

## PREPARING THE BUDGET DOCUMENT —WHAT IS INCLUDED?

After the City Board has approved the draft budget, the final draft is sent to the City Board for review and recommendation to the Council.

The budget, as this manual has emphasized, is more than a financial plan. The budget should also serve as a policy document, an operations guide, and a communication device. To achieve the multiple purposes of budgeting, the following should be included in the budget document:

- **Table of contents.** This helps the reader quickly locate items in the document
- **Budget message.** A message from the Mayor summarizes major revenues and expenditure proposals, explains significant changes (financial or programmatic) from current year to the budget year, and describes recommendations to address major issues and problems faced by the local government.
- **Financial policies and budget guidelines for the budget year.** Policies and guidelines depict the financial framework in which budget decisions are made and how the current budget responds to them.

- **Financial summaries and tables.** These include:

**Chief of the village of Apatzingán, Michoacán (1966-1970) (4 years)**

- **Investment program detail.** The document should contain program/project descriptions and sources of funds.

- history of the community and gmina
- demographics (land area, land use, population, median age, racial/ethnic composition, climate)
- economics (major employers, unemployment rates, taxes, etc.)
- public service statistics (airport, housing units, parks and green spaces, schools, etc.).

## PRACTICAL EXERCISE

The **thinkers** staff produced the **series** of **books** that **celebrates** the **evolution** of the **factoring** industry **from** its **early** **days** **to** **the** **present**. **Read** **it** **now**.

Why are you providing this document? Are there any changes in the budget document?

**Exhibit 11-1**  
**City of Krakow Budget**  
**Operating Budget Detail**  
**Task Budget Description**  
**[extract]**

|

**Exhibit 11-2**  
**City of Krakow Budget**  
**Budget Message - 1994 & 1995**

**Exhibit 11-3**  
**City of Lublin 1995 Budget**  
**Revenue and Expenditure Pie Charts, Bar Graphs, and Tables**  
**[extract]**

**Exhibit 11-4**  
**City of Szczecin Budget**  
**Citizen's Guide to the Budget**

|

**Exhibit 11-5**  
**Budget Document Evaluation**  
**How Does Your Budget Compare?**

## **Exhibit 11-5**

### **BUDGET DOCUMENT EVALUATION HOW DOES YOUR BUDGET COMPARE?**

#### **As a Policy Document**

1. Which of the following are included in your budget?
  - ☐ department or program objectives for the budget year (3 points)
  - ☐ organization-wide goals that span more than one budget (6 points)
  - ☐ both of the above (9 points)
2. What is included in the budget message?
  - ☐ summary of major revenues and spending proposals (3 points)
  - ☐ recommendations to address major issues and problems confronting your gmina (6 points)
  - ☐ themes that link policy issues with budget proposals (9 points)
  - ☐ all of the above (12 points)
3. What fiscal policies are included in your budget document?
  - ☐ financial policies that span more than one budget (e.g. debt policies) (3 points)
  - ☐ fiscal or budget guidelines pertaining to the current budget (6 points)
  - ☐ both of the above (9 points)

#### **As a Financial Plan**

4. What debt information is included in the budget?
  - ☐ estimate of current outstanding debt (3 points)
  - ☐ analysis of current debt capacity and its implication for the budget (6 points)
  - ☐ both of the above (9 points)
5. Which of the following financial summaries are included in your budget?
  - ☐ consolidated summary of revenues and expenditures for all budgeted funds (3 points)
  - ☐ summary of expenditures by department or program within fund type (6 points)
  - ☐ both of the above (9 points)
6. What type of revenue analysis is included in the document?
  - ☐ description of major revenue sources (3 points)
  - ☐ discussion of significant revenue trends and underlying assumptions for revenue estimates (6 points)
  - ☐ both of the above (9 points)
7. How detailed is the spending information presented for individual departments or programs?
  - ☐ more than five line items or objects of expenditure (1 point)
  - ☐ less than five line items or objects of expenditure (3 points)
  - ☐ expenditures by activity only (6 points)

8. What information does your operating budget include on major investments?  
\_\_\_ list of investment and their cost for the budget year (3 points)  
\_\_\_ estimated impact of investment projects on current and future operating budgets (6 points)  
\_\_\_ both of the above (9 points)
9. How many years of data are included in the financial summaries or program schedules?  
\_\_\_ one year (1 point)  
\_\_\_ two years (3 points)  
\_\_\_ three years (6 points)

### **As an Operations Guide**

10. How much information on department and program responsibilities is provided?  
\_\_\_ mission statement or statement of purpose for each department or program (1 point)  
\_\_\_ mission statement or statement of purpose for each major activity within a department or program (3 points)
11. What measures of performance are provided for departments or programs?  
\_\_\_ discussion of prior budget results and accomplishments (3 points)  
\_\_\_ one or two years of quantitative or qualitative performance data (9 points)  
\_\_\_ three years of quantitative or qualitative performance data (12 points)
12. What information is included in your budget on personnel or staff levels?  
\_\_\_ number of full-time equivalent positions by department or program (1 point)  
\_\_\_ number and type of full-time equivalent positions by department or program (3 points)  
\_\_\_ number and type of full-time equivalent positions for each of three years (6 points)
13. What is included in the organizational chart?  
\_\_\_ department (1 point)  
\_\_\_ department and programs/activities (3 points)  
\_\_\_ department, programs/activities, and position counts (6 points)

### **As a Communication Device**

14. Which of the following reader aids are included in your budget?  
\_\_\_ table of contents (1 point)  
\_\_\_ table of contents and glossary (3 points)  
\_\_\_ table of contents, glossary, and index (6 points)
15. What type of information is provided on the budget process?  
\_\_\_ description of budget phases and timetable (1 point)  
\_\_\_ description of budget phases, timetable, and roles of key participants (3 points)  
\_\_\_ description of budget phases, timetable, roles of key participants, and related financial planning systems (e.g. long-term investment plan) (6 points)

16. What type of visuals are included in your budget?
- ☐ graphs (e.g. line graphs, bar charts, pie charts) (1 point)
  - ☐ graphs and maps (3 points)
  - ☐ graphs, maps, and photographs (6 points)
17. Where are the graphs placed within the document?
- ☐ grouped together (1 point)
  - ☐ interspersed throughout the budget (3 points)
18. What information is provided on the community of population served by your jurisdiction?
- ☐ economic, demographic, or social statistics (1 point)
  - ☐ economic, demographic, or social statistics by geographic area or population sector (3 points)
19. What is included on the budget cover?
- ☐ title only (1 point)
  - ☐ title and artwork (e.g. design or photos) (3 points)
  - ☐ title and artwork in more than one color (6 points)
20. How is your budget summarized?
- ☐ summary within the budget document (1 point)
  - ☐ separate budget in brief or summary budget (6 points)
- ☐ Total Score

**Document scores** (Maximum score: 141 points)

37 to 67	Requires a major overhaul
68 to 98	Some sections may need major revisions
98 to 128	Could use some fine-tuning
+129	Looks like a budget award winner

## **CHAPTER 12**

# **INTEGRATING BUDGETING, ACCOUNTING, AND OTHER FINANCIAL SYSTEMS**

### **PURPOSE**

The purpose of this chapter is to enable you to:

- Identify the components of an integrated financial management system and list its benefits
- Explain the linkages between budgeting and other financial systems
- Identify strategies to implement an integrated financial management system
- Determine how your jurisdiction rates in its degree of integration.

### **HOW THIS CHAPTER WILL BENEFIT YOU**

Most of the material presented to you during this training workshop focuses on budgeting. Budgeting is an important part of local government decision-making; however, there are related parts of the financial management system that you should be aware of. Understanding the interdependency of these parts is important, as changes in one usually impact others. This chapter introduces you to the concept of an integrated financial management system and its benefits. You will also learn how budgeting and the other parts of the system are linked together. Understanding how these are interdependent will increase your understanding of the financial management system of local government.

### **FINANCIAL MANAGEMENT SYSTEM INTEGRATION-OVERVIEW**

Throughout this chapter, the term “financial management system” is used to refer to a computerized system. As local governments in Poland and other countries become responsible for a wider range of tasks as services to budget for and manage, it will be preferable to look toward a computerized system in order to take full advantage of available technology and to facilitate the full integration of the financial management functions. The particular computerized financial management system that your local government uses will depend upon the resources and needs of your jurisdiction. Resource constraints may limit the initial implementation of a full system, but having a plan for full implementation will help guide the step-by-step acquisition and use of equipment so that separate segments can be integrated as they are added.

## What Is an Integrated Financial System?

Local government can improve financial management by bringing four financial functions together as an integrated financial management system. An integrated financial system consists of four functional components:

- **Budgeting**—The process that allocates scarce resources among a host of competing demands and prepares and implements a local government's financial plan.
- **Accounting**—The basic financial record-keeping and expenditure control tool of local government that records, analyzes, and summarizes financial transactions and communicates the results of transactions for government.
- **Performance Measurement**—The improvement of public service delivery by establishing and monitoring targets for program performance. It often includes a focus on increasing productivity.
- **Auditing**—The process of evaluating the locality's fiscal and service operations. Auditing provides vital "feedback" to managers to improve control, management and budgeting.

These represent the four basic elements of the planning and control system through which local government operates to provide basic delivery of services. These elements are interrelated as part of the overall planning and control system shown in Exhibit 12-1. The overall system has the following components:

- **Decision-making**—The process begins with planning and analysis to make decisions about priorities, levels of program funding, work to be accomplished, and funding. Budgeting is the key component.
- **Implementation**—Management and control determine the operation of government during implementation. In this component, control systems keep expenditures within pre-defined limits, and managers stay informed about the delivery of public services. There are two control systems:
  - Accounting reports to management on actual expenditures to ensure that they are within budget, and
  - Performance reports to management on operations to ensure that service delivery is as expected.
- **Assessment**—Evaluation takes place after the activity is complete or at the end of a defined period to report to management whether results adhered to the targets. Two types of audits are used: financial compliance and program performance. Both are necessary for full evaluation.

This is how these components of an integrated financial management system are interrelated with the planning and control system through which a local government decides what to do, carries out its decisions, and modifies them based on feedback.

### **Why Is Integration Needed?**

In most local governments, these four functions (budgeting, accounting, performance measurement and auditing) are not adequately integrated, which causes problems in financial management. Some of the more common problems include:

- The system is fragmented. Staff are concerned only with their area of influence. Budget staff are concerned with budget preparation and expenditure control and have no interest in performance aspects of the budget. Accountants deal only with expenditure control and correct account codes.
- Decision-making is hampered by lack of information about program performance. Program information may not be gathered or is not adequate.
- Department and program managers are usually told what they can spend—not given what they need. While these limits are observed and generally enforced, the externally-imposed limits on spending tend to delay reporting and correction of emerging problems.
- Department and program managers generally are not told what they are expected to achieve. Performance is not measured, reported, monitored, or related to costs.
- The financial system may be periodically evaluated by financial and compliance audits, but there are rarely program performance audits.

Financial management problems have arisen because each function has evolved independently. Also, the purpose of local government financial management has been limited to expenditure control and reporting to higher levels of government. Creating functions that primarily serve the needs of local government has often been neglected.

### **Is Financial Integration Feasible?**

Integrating four functions into an effective planning and control system is not an easy task, but it is feasible. Other jurisdictions have accomplished it. Following are some observations from others who have undertaken the task of integrating their financial system:

- Top management support is essential.
- A significant commitment of resources is necessary—staff, consultants, hardware, and software.

- A substantial amount of time will be required.
- Expect resistance at all levels of the organization. People do not like change, and integration adds work to departments and agencies.

It is important to note that an integrated financial management system is more than a *financial* management system. When finances are integrated with performance, and decision-making with implementation, the result is an overall management (planning and control) system. There are many advantages of an integrated financial management system, but few of them come automatically. They depend on managerial efforts to maximize the benefits of an integrated system.

### **Why Sponsor a Financial Management System? Limited Resources in the**

Any significant investment of scarce staff, time, and money resources is an important decision, and the benefits from such an investment need to be quantified and considered prior to deciding. The benefits of an integrated financial system include:

- Increased opportunities to improve decision-making,
- More effective expenditure and performance control,
- Improved program management,
- Improved financial capabilities to meet increased reporting requirements from internal and external sources (program performance management, full cost recovery of user fees, or credit rating agencies),
- Increased discipline imposed upon finances and program performance, and
- Improved collection of historical program costs, effectiveness, and performance to support future spending decisions.

## **INTEGRATING BUDGETING AND OTHER FINANCIAL SYSTEMS**

Budgeting is the cornerstone of a financial management system because it is the process of allocating scarce resources among a host of competing demands and is the central element in decision-making. The previous chapters covered the various aspects of budgeting: phases of the budget cycle, multiple purposes of budgeting (control, management, planning and communication), and budget format types (line item, activity, program, and performance).

This section discusses the increased interrelationship of the budgeting function to accounting, performance management, and auditing. The evolution of budgeting from emphasis on expenditure control to multiple purposes—control, management, planning, and communication—increases the complexity and magnitude of demands placed upon the other three financial management functions. This increased interrelationship requires that each of these separate functions produce a higher quality product. To do otherwise impacts the total financial management system. As more local governments adopt program and performance budgeting to improve decision-making, the interrelationships become more critical.

## **Budgeting and Accounting**

Accounting performs two functions for budgeting: (1) it provides most of the information needed to monitor expenditures against the budget, and (2) it provides a control on spending to verify that expenditures are valid and comply with accounting policies and procedures of the local government. Each function has a significance for budgeting.

**The information function** . After the budget is adopted, the annual appropriations are entered into the accounting system. As transactions are recorded, they are posted to the appropriate accounting records and to the budget. The accounting system records transactions daily throughout the year and provides information reports on a regular basis (monthly) to present the status of revenues and expenditures to date versus budget. Without this information, budget staff would not be able to act on potential revenue shortfalls or the over-expenditure of appropriations. The accounting system and staff are responsible for providing this “Budget versus Actual” information for all revenues and expenditures on a monthly basis.

The accounting system must also provide current and past year information on program expenditures and costs that a manager might need for preparing next year’s budget. To carry out this reporting function, the accounting system must be capable of collecting and displaying this information in a form that budget staff can readily use. Unfortunately, not all accounting systems are flexible enough to produce reports for different purposes in different formats. Accounting systems tend to produce numbers and reports to show what was done with the money and to meet audit requirements. Budgeting, on the other hand, focuses on the functional programs or purposes for which the money is to be used.

Program and performance budgeting add significant complexity to the accounting system. For manual accounting systems, it is not feasible to record and keep track of another set of accounts while still fulfilling legal reporting requirements. In theory, these new budget demands can be accommodated in a computerized accounting system—but that assumes a considerable flexibility in accounting systems. Generally speaking, accounting systems have only had that flexibility built into them in the last five to ten years. Now, with the advent of PC based accounting systems, flexibility is a built-in consideration in most systems.

In some jurisdictions, accounting information has limited value to budget administration because it is not provided promptly, it is not available in the right categories to be useful, it has

significant delays in internal service billing or float between departments and central accounting, and it does not capture contract obligations not paid—encumbrances. The result is that budget reports would be misleading with expenditures understated.

**The control function** . The control of expenditures to ensure that appropriations are not exceeded is the responsibility of the accounting staff rather than the budget office in most instances. The accounting system provides additional control over contracts, purchase orders, and payroll so that invoices/bills will not be paid unless there is an available appropriation sufficient to cover the transaction. The accounting staff in reviewing and processing each transaction also ensure that each transaction is charged to the correct appropriation and account code and that they have properly approved and documented it. This control of transactions by the accounting staff ensures that information prepared from the accounting system records is accurate and reliable.

## **Budgeting and Performance Management**

Traditional budgets provide a financial plan that outlines what a local government expects to buy over a fiscal year and where the resources are going to come from. The expenditures are earmarked for a specific use: salaries, supplies, etc. In some cases expenditures may be further allocated to a specific program use: street cleaning, park maintenance, etc. The budget office's concern is to ensure that expenditures do not exceed available appropriations and that the overall budget stays within the existing limits. The focus is upon ensuring that these financial objectives are achieved at the end of the year.

A different but still important aspect of budgeting is to determine how those funds are used and what they achieved or produced. Resources might have been allocated to pave 25 kilometers of streets. If the 25 kilometers of streets were not paved as planned, then this too is considered not meeting a budget objective of a program. Failure to meet either a financial objective or a performance objective is reason for management to determine the need for corrective action.

Modern budgeting requires performance measures to help assess whether missions of public departments or agencies are accomplished. Linking performance measures to budget accounts is the most straightforward way to accomplish this assessment. Jurisdictions that have not added performance measures to the budgeting system are overlooking a significant part of a modern budgeting system.

## **Budgeting and Auditing**

Budgeting and auditing operate in two different time frames. Budgeting looks forward in time; auditing looks back to see what happened. The relationship of these components stems from these different time frames. There are two different kinds of audits that relate to the budget—the financial audit and the performance audit.

**Financial audit** . The compliance or financial audit is more traditional in local government. It may be performed by an internal auditor, or the services of an external auditor may be engaged. The financial audit's scope of work usually includes determining whether financial transactions have been properly reported and classified, whether internal controls are sufficient to justify confidence in the reports generated, and whether legal requirements have been met in the expenditure of funds. From these audits, management and the budget office gain useful insights into areas where procedures can be improved and controls tightened. Financial audits also provide assurance to elected officials, management, and the public about the soundness of the financial system.

**Performance audit** . The performance audit, also known as a management audit, is a relatively new type of audit. The performance-oriented audit examines whether public programs have met their performance objectives and determines how funds were applied to meet program objectives. The audit also provides the budget office with an independent assessment of a program's performance for future years. A performance audit usually recommends that changes be made to program operations to improve the effectiveness of the program or utilization of funds. Management and the budget office consider these recommendations in subsequent years' funding requests. Action plans are prepared by management to respond to audit recommendations.

## **STRATEGIES FOR INTEGRATING FINANCIAL SYSTEMS**

This section offers some general observations and suggestions related to developing or installing an integrated financial system. These apply both to local governments with financial management systems that only need minor system improvements and to those who may be developing an integrated financial management system for the first time. Each local government requires a strategy to successfully integrate their financial system.

### **Organization Issues**

Financial management is the center around which other management systems should be developed. As such, developing a financial management system should not be left only to the budget and accounting staff. Some suggestions for organizing the system development project include:

**Set up a financial management committee or task force** . This committee is purposely structured to include a wide range of participants. Include on the committee: the budget officer, the finance officer, the auditor, a member of the executive management team, the information systems officer, and representatives from major operating departments. It also may be beneficial to include the Chair of the Council Finance Committee or a similar representative from the Council. The mission of the committee is to develop policies and strategies, determine priorities, review proposed projects, and monitor progress of the installation.

A broad based committee can be very beneficial. It involves departments who have a vested interest in the project, those most affected by changes in workload, and executive management and political leadership. When problems arise with the project, the committee has a knowledgeable decision-maker to consult with and assist in resolving the issue. A committee is also an excellent way to maintain communication with the principals of the departments involved in the project throughout the local government.

**Staff the project** . Development or installation of a financial management system is a major undertaking. Depending upon an already over-committed existing staff is certain to be unsuccessful. Successful installations dedicate staff from accounting and budget offices to work on the project full-time. Also, full-time staff from Information Systems are needed throughout the project for computer systems support. Additional staff will be required as specific components are undertaken. If resources are limited, put fewer staff on the project . You should be aware, however, that having fewer staff to do the work results in slower progress on the project and may delay the system start date.

**Use consultants** . Most local governments installing a financial management system require consultants to do the work, augmented by local government staff. If local staff are limited, one solution is to hire additional consultants with the necessary skills. For many aspects of financial management system installations, local staff do not have the skills required. Consultants are necessary to supplement time and skills available from local staff.

If hiring consultants is the organizational strategy chosen, here are a few practical suggestions to consider:

- Identify at least three qualified firms or individuals for consideration and solicit proposals from all three.
- Request references from the consultant on work done for other comparable sized government installations and check their performance with those officials.
- Conduct interviews with the principals of the consultant's firm to discuss scope of work, cost, time frames, possible problems, and options.
- Include staff training, where appropriate, in the contract.

## **Identify Needs, Problems, Opportunities, and Issues**

With financial management systems, as with anything else, it is easier to get attention focused on an issue if the public believes there is a problem or a need. Since these systems are generally out of the public view, their problems and shortcomings may only be known to the people who use the system on a daily basis. This section identifies what to look for in determining if there is a problem with the existing financial management system.

Some of the financial problems might be known to the finance and management staff. These include:

- Failure to meet financial management reporting requirements for a program
- Deficiencies identified in a financial audit
- Spending in excess of appropriations in some programs
- Significant variances from budget in actual revenues or expenditures
- Complaints of long delays or suspension of contractor payments
- High delinquencies in major revenue sources.

Some financial problems will only become known with further investigation. These include:

- Substantial funds in non interest bearing accounts
- Delays in receipt and deposit of funds
- Unknown amounts of contractual obligations incurred but unpaid.

Another common problem is inadequate information on expenditures. This problem most often becomes apparent when public attention is focused on performance or service problems of a specific program or service. In such a case, you may request expenditure information on a specific program to see if you can determine where the problem lies. You will know that your information on expenditures is inadequate if your request is returned with the answer, "that information is not available in the financial system," or if the workload needed to find the answer means that critical city operations will come to a halt.

Another way to identify problems or needs of your financial management system is to ask the users of the system. Financial systems are usually designed to meet the accounting and reporting needs of the accounting staff. The needs of operating departments and program managers are rarely considered. When you ask these departments about their needs for a financial management system, you receive a different perspective. Operational needs should be considered as well.

Local governments need to identify opportunities to initiate changes in financial management systems if needed. These opportunities may be disguised as problems, but the response to the problem may be the opportunity. For example, a response to a serious financial debacle or scandal affecting the city or a program may require a systemic solution. A change in political or administrative leadership may create an interest in management reform and an opportunity for improving financial management systems.

It is also necessary to identify the deficiencies in the existing financial system, whether they are current problems or not. One way to do that is to compare the existing system capabilities to those of an integrated financial management system used by other similar sized jurisdictions. Another way is to identify two or three contractors who sell integrated financial management systems for governments and develop a list of capabilities for comparison based on their

systems. A third and possibly the easiest way to identify deficiencies is to use the elements of the integrated financial management system checklist included in Exhibit 12-2.

The completed inventory of problems, needs, and opportunities is used in documenting the need for an integrated financial management system, determining priorities, and developing a plan of action. If sufficiently detailed and documented, this step provides the justification for developing a financial management system.

## **Developing a Plan**

At this stage, few local governments are able to define a detailed development plan. However, it is important to establish a working framework of what must be accomplished and when. At a minimum, the initial plan should include the following:

- Outline the first steps, to be taken over the next year.
- Indicate how these steps are related to the elements of the financial improvement effort to be undertaken in subsequent years.
- Include in a comprehensive outline how the plan is to be accomplished (contractor, local staff, combination) and the time frames involved.
- Develop preliminary costs and expected recoveries and benefits; also, identify the needs and problems to be resolved.

The above lays out an initial plan, but there are many ways to accomplish this task. It is important to develop a plan consistent with the needs and procedures of your local government. The initial plan should be refined and detailed over time to adjust for unanticipated events. Following are some of the considerations which should be included in developing a plan and strategy:

- Avoid taking on more at any one time than can be done effectively.
- Concentrate individual steps in specific departments or functions. Concentrated efforts are more likely to be productive than government-wide approaches.
- Give priority to areas where there are known problems or opportunities.

Each local government should consider its own needs, priorities and opportunities in deciding where to begin to improve the performance of its financial management system. Some possible strategies are offered for consideration:

**Install a comprehensive financial management system** . Sometimes a financial debacle or crisis gives elected officials and management the impetus to make the significant

investment needed to fix their problems by developing a complete financial management system. Some local governments need a crisis to be prompted into action. More proactive local governments identify needs and problems before they become a crisis and act to develop a comprehensive financial management system in the normal course of improving government operations.

**Install one department at a time .** Installing a system one department at a time has the advantage of making the job more manageable and makes it easier to interrelate budgeting, accounting and performance management in that one department. Departments with supportive directors and competent staff can serve as pilot programs and help debug the system before it is extended to other departments. However, this approach means that two different systems need to be accommodated—the new system in the pilot department and the old one in all others.

**Install critical systems first .** In U.S. local governments, the most critical financial systems are budgeting, purchasing, and the general ledger accounting system. The strategy of installing these systems first recognizes the interdependence of budgeting, purchasing, and accounting. With this strategy, only one system is maintained at a time, and all departments are on the same system. Other modules of the integrated financial management system can be added at a later time as the organization adjusts to these improvements and is ready for enhancements like performance management. In a large organization, this installation of critical systems can be a significant undertaking depending upon the degree of decentralization.

**Install budget first .** Usually, budgeting is suggested as the place to start modernizing the financial management system. This strategy may achieve early improvements in decision-making if the accounting system can accommodate the changes. However, the changes envisioned for the budget (i.e. program budgeting) probably cannot be accommodated by the existing system and necessitate a new financial accounting system that can accommodate varied reporting requirements. Often, when system reform begins with budgeting, it also stops there.

**Begin with auditing .** This is a unique approach that begins by conducting a comprehensive independent audit. The audit results in a report outlining specific recommendations for improving the financial management system. Using an independent auditor to determine the need for these improvements commands a high degree of immediate credibility because of the auditor's independence and the relationship between audit findings and status of the city in financial markets. A disadvantage of this approach is that some executives may be uncomfortable with public exposure of financial management problems.

**Begin with performance management .** Starting here places emphasis on areas where there may be significant interest from the public and Council. However, unless there are strong linkages to the budgeting and accounting systems, starting here may require developing stand-alone reporting systems, defeating the purpose of an integrated financial management system.

**Project by project** . It is possible to begin a financial management improvement program by addressing needs, project by project, that are not necessarily closely related; however, the organization must consider how these will eventually tie together at a later date. The advantage of this approach is to implement improved financial management systems where there is the likelihood of the greatest savings or where politically important problems are addressed. The major disadvantage is that these dispersed efforts must ultimately be integrated into an overall comprehensive program.

## **Implement the Plan**

Assuming that the preparatory work received the approval of management and Council, attention turns to implementing the plan. Some strategies are offered to ensure that the plan is executed as scheduled.

**Continue the financial management system committee** . The committee, with its broad based membership, should remain active. Its mission should now focus on policy issues, monitoring implementation, resolving unanticipated problems, and keeping management and Council advised of the status of the project. They should meet regularly to stay informed of project changes and to act swiftly when problems come up.

**Develop a Gantt chart** . A Gantt chart sets out a critical path for all components of a project to be completed in order to complete the project in the shortest possible time. Developing a financial management system that affects all departments in a city is a significant undertaking. The complexity of the project is increased by the number of organizations involved, the number of people needing training, the number of different modules of a financial management system being developed and installed, the need for new equipment, and the time allotted to complete the project. Determining the optimum schedule for initiating and completing these activities is critical to a successful installation. A delay in any one area may significantly affect every other step thereafter and cause the project to miss critical deadlines.

**Establish a comprehensive training program** . It is critical that you emphasize training. Training plans need to consider who will conduct the training, who will train the trainers, what the training will consist of, who will develop training materials, where and when the training will be conducted, how many people will be trained on which systems, and how much time is required to accomplish the training. Ideally, a separate training facility should be set up. It should include both classroom and practical training using a prototype system. Training should be accomplished as close to the system change-over date as possible so staff will remember the training when the new system is installed and operational.

## **EXERCISE: FINANCIAL MANAGEMENT SYSTEM CHECKLIST**

Exhibit 12-2 contains a checklist to assess whether your jurisdiction is making progress toward a fully integrated financial management system.

Meeting the demanding standard of a fully integrated financial management system is not an easy task. First, the four components systems of budgeting, accounting, performance measurement, and auditing must be in place and operating. Second, the links between these basic functions are also considered in the assessment.

Do not be surprised if your jurisdiction fails to score high on any one of the components—especially if there has not been an effort to connect the systems. While the number of jurisdictions that have integrated financial systems is growing, few jurisdictions can claim to meet all these standards. What is important is to use the checklist as an indicator of how your jurisdiction compares against a demanding standard so that you can determine how much more you need to do to reach an integrated status.

**Exhibit 12-1**  
**Financial Management Inter-Relationships**

Budgeting

Decision-Making  
(Planning and Analysis)

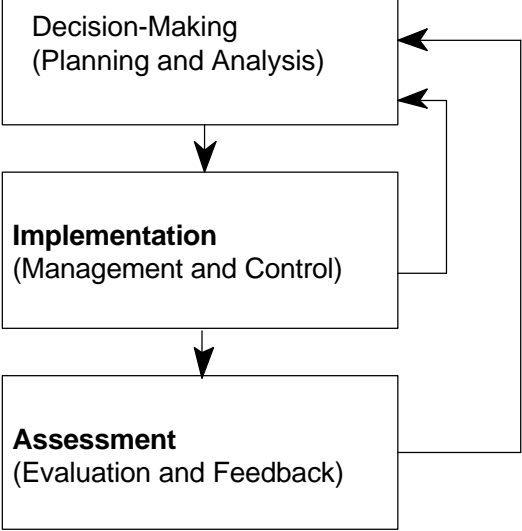
Accounting  
Performance  
Management

**Implementation**  
(Management and Control)

Auditing

**Assessment**  
(Evaluation and Feedback)

**Exhibit 12-1**  
**FINANCIAL MANAGEMEN**



**Exhibit 12-2**  
**Financial Management System Checklist**

## Exhibit 12-2

### FINANCIAL MANAGEMENT SYSTEM CHECKLIST

The purpose of this checklist is to provide a guide to help local government financial management auditors

Directions: Read each question and circle "yes" for those activities that your jurisdiction currently performs and "no" if your jurisdiction does not or if you do not know.

#### Budget

1. <i>Comprehensive Budget Coverage</i> . Does the budget cover all the funds expended by the local government?	Yes	No
1. <i>Budget Staff</i> . Is there a professional budget staff person or unit responsible to the chief executive that works for him/her in preparing the executive budget?	Yes	No
1. <i>Operating Budget: Revenues</i> . Is there an established procedure for developing and periodically updating estimates of revenues?	Yes	No
1. <i>Operating Budget: Expenditures by Program</i> . Is the operating budget formulated in terms of programs and activities (defined in terms of major purposes) rather than solely by organizational unit or objects of expenditure?	Yes	No
1. <i>Budget Analysis</i> . In the review of proposed department budgets, does the budget staff person or unit:		
Analyze program costs per unit of workload or service delivered?	Yes	No
Evaluate program benefits against costs?	Yes	No
Estimate future year expenditures for proposed new programs and activities?	Yes	No
1. <i>Capital Budget</i> . Is there a separate capital budget or separate capital component of a consolidated budget that lists individual capital projects and provides basic financial data on them?	Yes	No
1. Does the capital budget include estimates of the future impact of projects on the operating budget?	Yes	No
1. <i>Multi-Year Fiscal Planning</i> . Does the executive budget include a multi- year financial plan that covers:		
The Operating Budget?	Yes	No
The Capital Budget?	Yes	No

1. <i>Legislative Review.</i> Does the process leading up to the adoption of the budget(s) include examination of the executive budget by a fiscal staff person or unit responsible to the local legislature?	Yes	No
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**Budget Administration and Accounting**

1. <i>Budget Allotments.</i> After the budget has been approved, is spending authority allotted by periodic intervals (e.g. quarterly) during the fiscal year so that departments know their spending limits?	Yes	No
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1. <i>Responsibility Centers.</i> Are funds appropriated or allocated to the heads of organizational units so that financial and managerial authority are clearly integrated?	Yes	No
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1. <i>Budget Modification.</i> Are department heads or program managers authorized to reallocate funds within program appropriations (without coming back to the chief executive, budget staff, or legislative body for each change)?	Yes	No
---	-----	----

1. <i>Budget Control.</i> Are there periodic reports to the chief executive and local Council on actual expenditures, encumbrances, and revenues against the adopted budget plan?	Yes	No
---	-----	----

1. <i>Accounting Basis.</i> Does the accounting system operate on an accrual basis (modified as appropriate) for both revenues and expenditures?	Yes	No
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1. <i>Municipal Enterprises.</i> Does the municipality have full accrual accounting for its independent revenue-supported enterprises?	Yes	No
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1. <i>Internal Controls.</i> Are there written accounting procedures that clearly set forth a system of internal controls?	Yes	No
--	-----	----

1. <i>Accounting Schedule.</i> Are the financial reports of the government certified by a professional financial management association?	Yes	No
--	-----	----

1. <i>Flexible Account Structure.</i> Does the accounting system have the capacity to provide data on expenditures and encumbrances not merely for each appropriation but also for:		
---	--	--

Program elements and activities used in budget analysis and presentation?	Yes	No
---	-----	----

Projects financed under special grants?	Yes	No
---	-----	----

Major organizational divisions?	Yes	No
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Major geographic divisions of the locality?	Yes	No
---	-----	----

1. <i>Common Database.</i> Does the accounting system produce data on expenditures and encumbrances for the programs, activities, and projects for which performance measurement data are collected?	Yes	No
--	-----	----

1. <i>Cost accounting.</i> Is there a capacity to generate the data required to determine the full costs of individual programs, activities, and special projects?	Yes	No
--	-----	----

### **Performance Management**

1. <i>Central System.</i> Does the locality have a performance management system covering the activities of all or most of its operating departments?	Yes	No
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1. <i>Component Systems.</i> If there is not a comprehensive system, is there a system that covers one or more individual departments?	Yes	No
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1.*Contents of Systems.* Does the performance management system contain the following items:

Measures or indicators of workload for relevant programs, activities, and projects?	Yes	No
---	-----	----

Measures or indicators of output for relevant programs, activities, and projects?	Yes	No
---	-----	----

Measures or indicators of effectiveness or quality of performance?	Yes	No
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1. <i>Management Plan.</i> Is there a regularly produced plan that sets forth the performance/productivity targets on an annual or more frequent basis?	Yes	No
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1.*Performance Reporting.* Is there periodic reporting on progress against the targets set in the annual performance plan?

To the chief executive?	Yes	No
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To the public?	Yes	No
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1. <i>Management Projects and Assistance.</i> Are there staff assigned to help local departments undertake special improvement projects and activities?	Yes	No
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1. <i>Executive Management Participation.</i> Does the chief executive play an active part in reviewing the results of the performance/productivity program and in requiring department adherence to targets?	Yes	No
---	-----	----

1. <i>Linkages to Budgeting.</i> Is the performance management system integrated with the budget process?	Yes	No
---	-----	----

1.Are performance data systematically used in budgeting analysis and reported with expenditure data in the budget?	Yes	No
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1.Are performance targets and objectives related to recommended appropriations included in the budget?	Yes	No
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### **Audit**

1. <i>Periodic Audit.</i> Are the municipal accounting system and its records and procedures audited annually by an independent public accountant?	Yes	No
1. <i>Financial Audit.</i> In addition to the annual independent audit, does the local government retain qualified auditors (on a staff or consulting basis) to conduct periodic, in-depth reviews of the financial operations of selected municipal activities?	Yes	No
1. <i>Performance or Management Audits.</i> Does the municipality have a continuing program of audits (operated on a staff or consulting basis) of the economy and efficiency of performance and the results achieved in selected municipal activities?	Yes	No
1. <i>Audit Response.</i> Has a standard procedure been established for responding to financial and performance audits to ensure that there is adequate feedback into the budgetary process?	Yes	No
1. <i>Audit Planning.</i> Is a statement specifying scope and coverage prepared in advance of each audit?	Yes	No
1. <i>Budget Involvement.</i> Do the budget staff participate in planning or propose subjects for inclusion in the program of selected financial and/or performance audits?	Yes	No
1. <i>Accounting System Audit.</i> Does the annual independent audit provide for an assessment of the adequacy of the municipality's accounting system and the related internal controls?	Yes	No
1. <i>Performance Audit.</i> Is there a program for the periodic or selected audit of the performance management program?	Yes	No
<b>Total</b>	—	—

## **CHAPTER 13**

### **COMPUTERS IN FINANCE AND BUDGETING**

#### **PURPOSE**

The purpose of this chapter is to enable you to:

- Understand the technological and other changes impacting local government finance and budgeting
- Identify uses of computers in information processing
- Identify the value of computers in the workplace
- Identify uses of computers in local government finance and budgeting.

#### **HOW THIS CHAPTER WILL BENEFIT YOU**

Computers are revolutionizing the way private and public organizations do business. Local governments, too, as public organizations, are applying computer technology in new and exciting ways every day to anticipate and solve many common local government problems. Financial systems, with their traditional use of computers, can apply advances in computer technology that will provide information to a larger group of people, on a more timely basis, and with increased efficiency. If properly prepared, the information generated by such a financial system can be more effective in improving the quality of decision-making.

This chapter provides an overview of the use of computers in information processing and of computers' value and use in local government finance and budgeting. It describes briefly how computer applications have been applied to the finance and budget processes to improve the availability and timeliness of information and the quality of decision-making.

## **COMPUTER TECHNOLOGY AND OTHER CHANGES**

One of the traditional uses of the computer in government is to perform numerical calculations. This capability makes computers particularly applicable to the finance and budgeting function in local government. As a result, the first application of computers in a local government was often the installation of an accounting and budget system. For many years thereafter, accounting and budget systems were supported by large mainframes or minicomputers. This need for large computers tended to limit applications to systems designed by the data processing department that efficiently stored and manipulated large volumes of data. These systems performed calculations efficiently but were generally inflexible for reporting purposes and difficult to modify, as a computer programmer needed to rewrite the computer source code to make a single change. As software programs improved, desktop micro computers became available, and, most importantly, networking technology improved. The advent of desktop microcomputers increased the number of installed computers, uses, and potential users.

At the same time the technology changed, there has been an increased demand for local governments to lower business costs, improve public services, and become more efficient. Local governments, and particularly the finance function, can meet this challenge by increasing their reliance on computer technology and by applying it to specific problems common in local government finance and budgeting.

## **USES OF COMPUTERS IN INFORMATION PROCESSING**

Computers are used to perform six information processing tasks in local government finance and budgeting:

### **Record-Keeping**

Record-keeping is a primary and elementary task performed by computers. Record-keeping involves the entry, updating, and storage of data. For example, the record-keeping function includes maintaining and updating files on citizen requests for service, personnel, or businesses, or files for financial information such as payroll, property tax records, accounting, inventory, or fixed assets.

## **Calculating and Printing**

Computers can arrange, select, calculate, and print stored data to produce specific information needed for a report, in any pre-determined format or timeframe. For example, computers are used extensively to process payroll, send bills to customers, prepare mailing lists, and prepare budgets. They have automated the process of preparing spreadsheets, replacing manual calculations for such time-consuming projects as calculating a department's employee salary and benefit costs, debt schedule amortization, and cash flow projections.

## **Record Searches**

While computers have significant data storage capabilities, they can also access and retrieve records with speed and accuracy. Computers can search thousands of records in fractions of a second to find a specific one or set of records that meet specific parameters. This quick response benefits customers by reducing wait time and increasing the efficiency of the person waiting on them. For example, customer service representatives use computers to access a customer's account instantaneously and to respond to a customer inquiry about a payment's status on the telephone or in person within seconds.

## **Record Restructuring**

Restructuring is the process of disassembling, reorganizing, and reassembling data in a new structure. It may also include an analysis of information. For example, the computer can use a crosswalk or matrix system to convert data from one type of budgeting format to another, i.e. from a state-required report format to a management-oriented, task budgeting format.

## **Analysis**

Computers programmed to manipulate data with multiple interrelated variables provide organizations with a useful analytic tool. The use of multiple regression modeling to forecast revenues is a specific example of computer analysis. Using statistical software to determine correlation between variables and then using the results of this analysis to plot trend lines of specific revenue sources is another example of using the computer as an analytic tool.

## **Control Processes**

Computers are used to monitor and control systems. The computer is given data that establish the parameters of the system monitored and is given instructions to initiate certain actions when those parameters, or limits, are reached. The computer may be programmed to shut down an operation to avoid a fire, explosion, or other catastrophe in an emergency situation. In less critical situations, such as budgeting, computers monitor appropriations. Computers are programmed to reject expenditure transactions that if approved would exceed appropriations, or to suspend the transaction until further approval or instructions are received from accounting or budget officials. In other ways, control processes improve the integrity and accuracy of the data in the financial system by screening transaction data to ensure that they meet certain pre-determined criteria and rejecting transactions that do not.

## **VALUE OF COMPUTERS IN THE WORK PLACE**

The increasing investment in and proliferation of computers in business and government has generated discussion about the value of computers and the degree they contribute to increased efficiency, effectiveness, and productivity of the employee.

Traditional claims of the advantages of using computers and information processing are numerous and varied. Computers are assumed to benefit organizations by:

- reducing costs and staffing due to the reduced need for personnel to manipulate data manually and repetitively,
- processing large volumes of information that would have been impossible before computerization,
- providing better information to managers and decision-makers,
- improving the ability of supervisors to supervise the work of subordinates,
- facilitating long-range organizational planning and analysis, thereby enabling the organization to prepare for future demands, and
- facilitating innovation adoption by transferring computer technology to other departments of an organization or to another organization (such as a local government).

Although many computers have been purchased and installed on the expectation that savings and increased productivity would result, the degree to which all these claimed advantages have been achieved is somewhat unclear. To clarify the issue, a survey of computer

users in selected city and county governments in the U.S. was conducted. The survey asked local government computer users about these traditionally assumed advantages. The findings from that survey provide a different perspective of what actually happens when computers and information processing are installed in local governments.

- **Reduced personnel?** The survey revealed that staff reductions were the exception rather than the rule. What normally happened is that the staff remained the same, but the number of transactions processed by the staff increased after computer installation.

- **Reduced cost?** The assumption that installation of computers will reduce cost is linked to the above item in which personnel are reduced. What often happens is that computer usage leads the organization to undertake new activities that it was not able to perform previously. The new activities generally absorb any cost reductions.

- **Better information for managers and decision-makers to improve decisions?** The survey revealed that computer information, properly used, could improve the quality of information available to management and the actual quality of decisions. However, computer information systems tend to grow over time and add additional data that may lead to information overload for decision-makers. Additionally, while information systems can aggregate and summarize data easily, the ease and speed of data retrieval cannot compensate for inaccurate or poor quality data. Users of computer information need to be concerned about the quality and accuracy of the data entered into the computer if they are to rely on the output.

- **Enhance supervisors' ability to monitor subordinates?** The survey confirmed that a supervisor could more closely monitor a subordinate's activities and performance. However, there may be adverse consequences: the employee may experience alienation and resentment because of this new oversight, and these feelings may negate the benefit.

- **Do computer information systems facilitate planning for organizational needs?** Actually, information systems add requirements for the organization to hire and retain qualified personnel to maintain an ever-increasing array of complex information systems. The survey revealed that numerous restrictions on local governments limit their ability to respond to these organizational needs. For example, government restrictions limit hiring, promotions, and salary levels. Often these restrictions make local government salaries non-competitive with the private sector market. Without competitive salary structures for computer trained personnel, local governments can only retain mediocre technical staff who do not effectively respond to the information processing needs of the organization.

- **Are innovative computer software programs transferred to other organizations to duplication of effort?** The survey indicated that such transfers rarely occur among local government organizations. The major reasons that software is not transferred are inadequate documentation, different city requirements, and incompatible computer systems.

In summary, installing computers in the workplace has produced a somewhat different set of benefits than traditionally claimed. Computer usage enables personnel to produce more work at lower unit cost, manipulate larger volumes of data and produce more information than was possible before computers, and improve the quality of information available to management and policy-makers to guide their decisions.

## **USE OF COMPUTERS IN FINANCE AND BUDGETING**

Computerization continues to increase throughout local government, and in finance departments specifically. In 1977, almost all of the U.S. cities and counties with a population over 100,000 used computers in their local government, and over 50 percent of the cities and counties with a population over 10,000 used them. Personal computers, integrated financial accounting systems, networks, improved software, and lower costs have increased the number of computer users in local governments and have allowed smaller local governments to purchase computers and integrated financial accounting systems for the first time.

The accounting system has been one of the primary uses of computer technology in local government. Accounting systems continue to grow in complexity and command a significant portion of the computer resources as additional accounting and finance sub-systems are integrated into the basic system. Modern integrated financial accounting systems now enhance the basic accounting system with modules for payroll, fixed assets, accounts payable, accounts receivable, budget reporting, encumbrance/purchase order, and external database interface systems. The user can choose modules to form a complex or simple accounting system according to the government's accounting needs. Computer software vendors have also continued the integration trend by linking the financial accounting system with other major systems such as revenue management, human resources, and material management. When systems are integrated, the financial accounting system works with the others to share data and functions without duplication. Integration of the financial system is important to computer use in local governments because it eliminates redundancy, resulting in reduced computer data storage space; easier access to detailed data; and timely, more accurate information. Properly used, more timely information leads to improved decision-making.

Benefits to local governments from integrated financial information and accounting systems increase when computers are linked together with local area networks (LANs). A LAN is a group of computers and associated peripherals linked by cables and sophisticated software packages. The LAN allows the user to access both the files stored in and the peripherals attached to another computer in the network. Computers and communications networks transport information in electronic form among individuals.

Information is the essence of many government services. Employees need large quantities of information to perform their jobs. To gain access to and process information, local government employees have an increasing number of devices, such as fax machines, desktop

and laptop computers, mainframe computers, handheld computers, stationary and mobile telephones, and pagers. Only when information is made available to others who can use it does it become valuable. Making information available to anyone who needs it, regardless of location or time of day, is the mission of computing/communication networks.

Computers and telecommunication networks are used in everyday financial management. Some of these uses are described below:

### **Revenue Administration**

Revenue administration uses all of the six capacities of computers—record-keeping, calculating and printing, record searching, record restructuring, analysis, and process control. Customer records are maintained by account for each revenue source or tax source. Based on these records, bills are calculated, printed, and sent to customers. If bills are sent out at different times and in groups to maximize cash flow, the computer needs to search for records and prepare bills for the billing period. Additionally, records are searched to determine a list of high dollar delinquent accounts that are given priority in delinquent collections. Records restructuring is used to relate customer records from one revenue file to the same customer of another revenue source. For example, a citizen may have separate records for a vehicle, a water account, and a small business. For collection purposes, it would be beneficial to know that these three accounts are for the same individual. Analysis is used to forecast long-range revenue trends. Statistical modeling and regression analysis are used to forecast revenue sources based on economic trends. Lastly, process control is used in systematically updating revenue receipts and monitoring collections against expected levels of performance. This control system provides an early notice of potential revenue shortfalls, should collections not reach expected levels.

### **Budget Planning and Analysis**

Budget planning uses records retained for other purposes, restructures them, uses financial tools to manipulate variables, and forecasts future revenues based on the results of analysis. Using the computer for these tasks significantly aids long-range financial planning.

### **Budget Preparation**

Almost all local governments use computers in budget preparation. The computer-assisted tasks vary with each government. Budget offices use the computer to:

- Create budget forms on which departments submit data to the budget office,
- Receive information from departments. This means that budget information is keyed into the computer only one time at the department and is then transferred electronically over telephone leased lines or fiber optic cable or on diskette to the budget office.

- Print the budget document and aggregate summary data quickly and accurately.

Other local governments, using a budget preparation module in an integrated financial accounting system, create alternative budget scenarios. This module provides the capability to construct a new budget based on historical budget or actual data. A budget worksheet can be created based on these data and then modified on a percentage basis (to allow for inflation, for example) or by adding or subtracting specified amounts. Once the budget is approved, the module automatically converts the budget worksheet into budget entries and loads them directly into the accounting system without re-keying.

## **Budget Presentation**

Many of the latest microcomputers now have sufficient memory to handle graphics software. Including tables, charts, and graphs in the budget can enhance the budget's attractiveness and readability. Software is also available to convert the budget into a formal presentation, complete with 35 mm slides or overhead transparencies and presentation handouts.

## **Budget Implementation**

Annual appropriations are usually divided into monthly or quarterly allotments. This is done to plan the orderly expenditure of monies consistent with available revenues. When revenues are received, these monies may be transferred to departments in proportion to their allotment. Computers programmed with these allotment percentages make the necessary calculations and transfers quickly and accurately.

Computers also support budget implementation and monitoring processes. Spending is monitored through an accounting system to ensure that expenditures do not exceed the appropriation established by the Council. Process monitoring is largely made possible through the use of the computer. Furthermore, computerization of the accounting system makes possible the accurate storage and rapid retrieval of large volumes of detailed financial data. With computerized information systems, data break-out and summaries needed in the budget implementation phase can be provided easily.

## **Auditing**

Computers can assist in the random selection of records or items to be physically matched with electronically stored data. For instance, a computer-assisted random selection of vouchers then may be examined with computerized records on expenditures to make sure that the physical and electronic records are in agreement.

## **Program Evaluation**

To evaluate programs, record-keeping of files on program inputs and outputs is necessary. Computerized statistical analysis facilitates the linking of inputs to outputs to determine if programs are having the desired effect.

## **Budget Reform**

Most budget reforms such as program budgeting would be difficult, if not impossible, to implement without computerization. Program budgeting has attempted to increase the rationality and efficiency of the budget process. Programs require the manipulation of large volumes of information, which would not be feasible in the timeframe of the annual budget cycle without computers. Since most governments in the U.S. use program budgeting in addition to object of expenditure budgeting, computerized crosswalk routines are needed to rapidly restructure budget information from one format to the other. The situation in Krakow is similar, as Krakow's use of task budgeting requires a computerized crosswalk routine to connect with the state's obligatory budget format.

## **FUTURE USES OF COMPUTERS**

Computers continue to revolutionize local government finance and budget processes. The impact of computerization will continue to be felt throughout local government in future years.

Personal computers, improved software, and extensive networks will facilitate the dissemination of information and computer technology throughout local government. Because personal computers are becoming more powerful, more user friendly, and less costly, they will be more widely used and will become an essential tool for all analysts. Computerization will fundamentally alter the power structure in the budgetary process and in local government itself.

The budget office will not be the only department with personal computers. Operational departments will have computers to maintain their own records, which can be used to develop their budget and, if needed, verify the information of the budget office. Power will be more decentralized than in the previous years. Participation, however, should also be decentralized, increasing the amount and quality of information available to all budget process participants. Equally significant, efficiency and accountability of the budget process should increase.

## **EXAMPLES**

These examples of various computer and spreadsheet applications for budgeting are drawn from Polish and U.S. cities.

Exhibit 13-1 illustrates the use of a computer spreadsheet to track a city's historical tax collection performance. This information is used to calculate a three or four year average collection percentage. The resulting collection average is applied to total property taxes to determine the amount that will be collected in the next budget year and included in the budget. Prior year taxes, penalties, and interest are also projected for budget purposes based on historical collection experience.

Exhibit 13-2 illustrates the use of a computer spreadsheet to record historic monthly sales tax payments from the state. Using a historically based collections percentage and dividing that percentage into the amount of current collections will produce a estimated projection of sales tax revenues to be received by year end.

**Exhibit 13-1**  
**City of Dallas**  
**Property Tax Revenue Projection Worksheet**

**Exhibit 13-2**  
**City of Dallas**  
**Sales Tax Collection Monitoring**

## **CHAPTER 14**

### **BUDGET APPROVAL AND EXECUTION**

#### **PURPOSE**

The purpose of this chapter is to enable you to:

- Understand what role the Council plays in the budget process
- Identify elements that should be included in a budget resolution
- Identify and describe the stages of budget execution
- Identify tasks needed to control expenditures and monitor the budget.

#### **HOW THIS CHAPTER WILL BENEFIT YOU**

Planning, preparing, and improving the budget process is a significant undertaking. However, these efforts will be wasted unless the approved budget is used to guide spending throughout the fiscal year. The budget guides spending in two ways: it limits certain program expenditures and at the same times authorizes spending for new or existing programs and activities. It is also important to remember that the budget is a plan based on estimates. Because estimates can be inaccurate, close monitoring of the budget plan's execution is essential.

This chapter briefly discusses the Council role in the budget approval process. It reviews basic elements of budget execution and emphasizes the importance of control and management of the process. The chapter lists the procedures and tasks needed to accomplish budget execution and provides examples of monitoring reports used in other gminas.

#### **COUNCIL REVIEW AND APPROVAL**

Upon receiving the recommended draft budget from the City Board, the Council reviews it, makes changes as needed, and ultimately approves it. Approval of a budget resolution establishes the legal authority for the gmina to incur expenses in the new fiscal year.

To review the draft budget, the Council refers the document to the budget committee of the Council. If a standing committee of the Council does not exist, the Council may appoint a budget review committee. The committee reviews the draft budget to ensure that it responds to Council budget guidelines and program priorities and determines if any changes are needed before it is considered and approved by the Council. If acceptable, the committee recommends that the Council approve the budget resolution as is, or if not, the committee recommends that the Council approve the budget resolution with changes.

The Council considers the budget resolution at a regular ly called public meeting. The Council's approval of the budget resolution completes the preparation phase of the budget cycle and adopts an Annual Plan of Income and Expenditures for the city effective January 1. The Council approves a budget resolution and attachments detailing the budget prescribed by Polish budget law. The attachments detail the gmina's plan of income and expenditures using the central government's standard classification of account codes (sections, chapters, paragraphs, etc.).

## **BUDGET RESOLUTION**

The budget resolution, approved by Council, serves two purposes. First, it approves specific incomes and expenditure levels for the gmina and other off-budget units. Second, it establishes policies for budget execution.

More specifically, the approved budget resolution details the income (including subsidies and grants) and expenditure levels for the operation of the gmina for the new fiscal year. It specifies investment plans and contingency reserve levels. Furthermore, the resolution approves the revenue and expenditures of units carrying out activities outside the budget.

The budget resolution may also provide the City Board with additional flexibility and authority to execute the budget within limits and policy guidance to manage the budget throughout the fiscal year. For example, the Krakow City Council budget resolution authorizes the following:

- a target reserve fund to respond to district council priorities, tasks of pilot programs, and investment initiatives and procedures for accessing the funds
- funding for programs that are demand sensitive (children involved in physical education and recreation associations) with stated distribution formulas

- establishing the authority of the City Board concerning increased funding of investment and renovation projects
- establishing the City Board's authority to financially obligate the gmina
- delegating specific authority to the City Board to execute the budget within limits set by Council
- establishing a requirement for the City Board to report on actions delegated by Council and the status of the gmina budget and finances semi-annually
- setting the number of authorized positions in Krakow City Hall and some exceptions.

With these additional provisions, the Council provides the City Board with specific policy guidance on budget execution. This is extremely helpful to management because of the clarity it brings to managing the budget execution process. Exhibit 14-1 contains the full text of the Krakow budget resolution for the 1995 budget. Contrast this resolution with the simpler budget resolution from the small gmina of Miedzna in Exhibit 14-2.

## **BUDGET EXECUTION**

Approval of the budget resolution opens, at the start of the fiscal year, the budget execution phase. The budget execution phase focuses upon control in carrying out the budget plans approved by the Council and City Board. The Treasurer is responsible for establishing procedures to ensure that expenditures comply with the budget, are properly authorized and accounted for, and are monitored against the budget plan.

Under the Treasurer's direction, the budget and finance departments prepare the gmina for the start of a new fiscal year from a financial standpoint. This usually means:

- producing copies of the approved budget for Council and City Board and departments responsible for monitoring budget execution
- preparing a budget summary for the public and media
- distributing other copies of the budget to organizations and enterprise units responsible for delivering services to the public
- loading the budget plan into the city's accounting system as soon as possible after the start of the fiscal year and initiating a budget monitoring system.

Although these are mundane tasks, they are an essential part of starting the fiscal new year and putting the budget control systems in place.

Budget execution practices and terminology may vary among local governments, but the basic elements of budget execution do not. Most gminas use these budget execution tools on an everyday basis to manage the budget. Budget execution usually consists of five stages:

- **Authorization** is the law or statute that permits spending for a specified purpose. Governments can only spend money for activities they are legally permitted to carry out.
- **Appropriation** is the legal authority to expend up to a certain amount of funds during the budget period. For most local governments, the annual budget document is the source for all or most appropriations. The Council approves the budget by adopting an ordinance or approving a resolution depending upon legal requirements.
- **Allocations** may be used by the City Board to provide further detail to the appropriation approved by the Council. The Krakow budget resolution, for example, appears to grant authority to allocate funds to certain programs based on a formula or other means.
- **Allotments** divide appropriations or allocations into periods such as quarters or months of the fiscal year covered by the approved budget. The allotment device is critical to ensuring that spending is carried out according to the budget. Allotment also helps ensure that monies are available to fund operations throughout the fiscal year. Finally, the use of allotments provides an “early warning” system when spending does deviate from the plans approved at the beginning of the fiscal year.
- **Adjustments** may be necessary as revenues and/or expenditures vary from projections contained in the budget document. Procedures for making adjustments (or transfers of budgetary funds) vary from gmina to gmina. For example, the Krakow City Board is authorized by budget resolution to carry out transfers of budgetary funds between chapters and paragraphs with some exceptions (see Exhibit 14-1).

## **EXPENDITURE CONTROLS AND MONITORING**

After completing the start-up tasks at the beginning of the fiscal year, the accounting and finance department staff support the Treasurer in controlling and monitoring budget execution by establishing procedures and accomplishing the following tasks:

- establishing monthly allotments of central government subsidies to appropriate organizational units
- ensuring the correct execution of the budget by reviewing the applications of departments concerning activation of funds and ensuring that units account correctly for funds allocated
- preparing resolutions for Council and City Board consideration/approval regarding changes in the budget or transfers of funds for unit activities
- reporting actual expenditures against the budget plan semi-annually or more frequently as directed by City Board
- reporting progress on accomplishments of task objectives and results semi-annually or more frequently as directed by City Board
- monitoring and reporting revenue receipts against the budget plan and instituting procedures should a revenue “shortfall” be forecast to occur.

## **EXAMPLES**

Extracts of selected cities' budget monitoring reports are included as Exhibit 14-3, City of Lublin; Exhibit 14-4, City of Szczecin; and Exhibit 14-5, City of Krakow.

## **PRACTICAL EXERCISE**

Participants will be divided into three groups and asked to discuss and answer the following questions and report their answers to the group.

### **Group I**

- What advantages are there to preparing a budget status report as shown in Exhibits 14-3 – 14-5?
- What are the disadvantages?

### **Group II**

- From a budget management perspective, would you change the report? Create a new one?
- If so, how would you change the report? What would you include in a new report?
- Why?

### **Group III**

The instructor will provide additional direction to Group III regarding the following questions.

- What information and tools would you need to implement a different budget reporting and management system?
- What advantages are there to the new budget reporting and management system?
- What are the disadvantages?

**Exhibit 14-1**  
**Krakow City Council**  
**1995 Budget Resolution**

**Exhibit 14-2**  
**Miedzna City Council**  
**1995 Budget Resolution**

**Exhibit 14-3**  
**City of Lublin**  
**Budget Monitoring Report**  
**September 30, 1995**  
**[extract]**

**Exhibit 14-4**  
**City of Szczecin**  
**Budget Monitoring Report**  
**June 30, 1995**  
**[extract]**

**Exhibit 14-5**  
**City of Krakow**  
**Budget Monitoring Report**  
**[extract]**

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